91-1707 (4)

No. _____

Supreme Court, U.S.
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In The

# Supreme Court of the United States

October Term, 1991

IN RE
UNITED SERVICES AUTOMOBILE ASSOCIATION,

*Petitioner*

**Petition For Writ Of Mandamus, Prohibition Or Other Appropriate Remedy To The United States District Court Central District of California**

**Petition For Writ Of Mandamus**
**APPENDIX, VOLUME III**
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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. 91 3615 WFN<br><br>PLAINTIFFS' SUPPLEMENTAL BRIEFING AS ORDERED BY COURT IN OPPOSITION TO MOTION TO DISMISS AND IN SUPPORT OF REQUEST FOR SANCTIONS<br><br>(Judge Wm. Fremming Nielsen) |

TO ALL PARTIES AND TO THEIR ATTORNEYS OF RECORD:

Plaintiffs LAUGHLIN E. WATERS and VOULA D. WATERS hereby submit their supplemental Points and

Authorities as ordered by the Court in opposition to the Motion to Dismiss of defendant UNITED SERVICES AUTOMOBILE ASSOCIATION ("USAA") and in support of plaintiffs' request for sanctions.

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1.

## THIS COURT SHOULD AWARD SANCTIONS UNDER ITS INHERENT POWER TO PUNISH USAA FOR ITS ABUSE OF THE JUDICIAL PROCESS

A federal court has several sources of power for imposition of sanctions on a party. First, the court may award sanctions under FRCP 11 which provides that all papers submitted must be signed, attesting to the fact that the paper is well grounded in fact, is warranted by existing law and that it is not interposed for an improper purpose. Violation of that rule permits the court to impose sanctions against the party or its counsel and the sanctions may *include* the opposing party's reasonable attorney's fees and costs incurred as the result of the filing.

Second, a federal court may impose sanctions under 28 U.S.C. section 1927 against an attorney for the excess costs, expenses and attorney's fees reasonably incurred by the other party as the result of conduct which unreasonably or vexatiously multiplies the proceedings in any case.

Finally, the federal court has the inherent power to impose sanctions on a party. In *Roadway Exp., Inc. v. Piper,* 447 U.S. 752, 766, 100 S.Ct. 2455, 2464, 65 L.Ed.2d 488 (1980), the United States Supreme Court quoted its earlier decision in *Alyeska Pipeline Co. v. Wilderness Society,* 421 U.S. 240, 257, 95 S.Ct. 1612, 1621, 44 L.Ed.2d 141 (1975) and noted that federal courts have the inherent power to punish for the willful disobedience of a court order or when the party has acted in bad faith, vexatiously, wantonly or for oppressive reasons.

Under its inherent power, the court may impose sanctions which may include payment of the other party's attorney's fees (*Roadway, supra*) or, even more critically, *reimbursement to the court or government for costs incurred due to the party's bad faith conduct. Eash v. Riggins Trucking, Inc.*, 757 F.2d 557 (3rd Cir. 1985). Additionally, the court may impose the sanctions against the client on the theory that the client is responsible for the conduct of the attorney's litigation. *Cannon v. Loyola Univ. of Chicago*, 784 F.2d 777, 782 (7th Cir. 1986). Given USAA's use of various attorneys throughout the country, it is obvious that USAA was the "brains" behind the manipulation of the federal courts and should properly be personally exposed to the payment of sanctions.

A. Sanctions against USAA are properly awardable under this Court's inherent power.

An exhaustive examination of the court's inherent power to sanction is presented in *Eash v. Riggins Trucking Inc.*, 757 F.2d 557 (3rd Cir. 1985). In *Eash*, an attorney was sanctioned in the amount necessary to pay the government's costs in impanelling a jury for one day for his alleged misconduct in failing to settle an action prior to the day of trial. Although the plaintiff had made several attempts to settle the case, no settlement was reached until the day of trial and the trial court apparently believed that the settlement was achieved at that point only because the defense attorney had a scheduling conflict.

The attorney appealed the sanction award and the appellate court remanded in order that the attorney be

given notice and opportunity to be heard in regard to the sanction matter. However, in doing so, the *Eash* court overruled its prior decision in *Gamble v. Pope and Talbot, Inc.*, 307 F.2d 729 (3rd Cir. 1962) which precluded such an award of sanctions under the inherent power, in part because of the extensive criticism the decision had garnered from other courts and treatise writers. The *Eash* court noted:

> A major factor in the decisions that have refused to follow *Gamble* has been the startling increase in the number and complexity of cases filed in the federal courts. The dramatic rise in litigation in the last decade has led trial judges to conclude that indulgent toleration of lawyers' misconduct is simply a luxury the federal court system no longer can afford. See *Renfrew, supra*, 67 Calif.L.Rev. at 275-276. Chief Justice Burger has recently observed that "a small handful [of lawyers] must not be permitted to abuse the system and preempt its time and machinery for purposes not intended, thus delaying and denying" access to courts to others in need of the courts' limited resources.

The *Eash* court relied on the Supreme Court's decisions in both *Roadway* and *Link v. Wabash Railroad Co.*, 370 U.S. 626, 82 S.Ct. 1386, 8 L.Ed.2d 734 (1962) for the existence of the court's inherent power to sanction. As quoted from *Link, supra*, 370 U.S. at 630-631, 82 S.Ct. at 1388-1389, the *Eash* court noted:

> the "inherent power" to sanction an attorney was "governed not by rule or statute but by the control necessarily vested in courts to manage their own affairs so as to achieve the orderly

> and expeditious disposition of cases." *Eash, supra*, 757 F.2d at 567.

Similarly, in *Roadway*, the Supreme Court permitted taxing of attorney fees directly against an opposing attorney emphasizing "the well acknowledged inherent power of a court to levy a reasonable sanction in response to abusive litigation practices." *Eash, supra*, 757 F.2d at 568.

The standards for application of sanctions under the court's inherent power were stated by the court in *In Re Itel Securities Litigation*, 791 F.2d 672 (9th Cir. 1986.) There, the court noted that:

> [t]he imposition of sanctions under the inherent power of the court is proper where counsel has " 'willfull[y] abuse[d] judicial process' or otherwise conducted litigation in bad faith." . . . For purposes of imposing sanctions under the inherent power of the court, a finding of bad faith "does not require that the legal and factual basis for the action prove totally frivolous; where a litigant is substantially motivated by vindictiveness, obduracy, or *mala fides*, the assertion of a colorable claim will not bar the assessment of attorney's fees. *Itel*, 791 F.2d at 675.

In *Itel*, the attorney for a group of bondholders making claims against Itel intervened in the securities litigation as a plan of extortion in order to obtain fee concessions in the bondholders' separate action, which had already been resolved. The trial court imposed sanctions of $10,000 in favor of the class plaintiffs and $5000 in favor of Itel. The appellate court affirmed and found that, as noted above, the attorney's conduct in the present action was improper, based on the fact that his relief was properly obtainable in the other action. The court further

held that, again as noted in the quote above, the fact that his intervention in the securities litigation may not have been meritless did not preclude the finding of bad faith.

In the present case, even if USAA's contention that it is an unincorporated association has some merit, its failure to disclose to this court its past representations that it was a corporate or corporate-like entity for purposes of diversity jurisdiction displays its bad faith conduct. The court in *In Re Ronco, Inc.*, 838 F.2d 212 (7th Cir. 1988) made clear that the failure to make a full and complete disclosure to the Court is a proper basis for imposition of sanctions.

In *Ronco*, counsel for a bankrupt was appointed to represent the Creditors' Committee and opposed a motion to determine the validity of certain creditor's liens. That counsel appealed the bankruptcy court's decision to the district court, claiming that its recent appointment as special counsel to the Committee had left it too little time to properly oppose the motion. The district court affirmed the bankruptcy court's determination and imposed sanctions, in part because the counsel failed to disclose certain information: Counsel did not disclose that it had previously represented a single unsecured creditor in the bankruptcy prior to its representation of the Creditors' Committee and that it had worked on the creditor's lien motion prior to being appointed as special counsel. The *Ronco* court noted:

> While the appellant did not misstate an empirical fact, it did omit facts that were highly relevant to an accurate characterization of the facts that were stated. Such an obvious omission

> placed a heavy burden on a court. The presentation amounts, in its totality, to a half-truth that can be just as misleading, sometimes more misleading, than an absolutely false representation. For purposes of determining whether sanctions are appropriate, it is not relevant that later submission by the appellees brought the truth to light. . . . The impact on the court and on the opposing party occurs when the initial omission is made. Later correction does not permit a recoupment of the time, energy or, in some cases, money that has already been expended. *Ronco, supra*, 838 F.2d at 218.

Just as the appellants in *Ronco* did, USAA provided this Court with a half-truth, an omission of critical facts, when it filed its motion to dismiss. USAA argued, in wide-eyed innocence, that it was an unincorporated association and not subject to diversity jurisdiction in this case, while hiding from the court the fact that it had, numerous times in the past, itself invoked such diversity jurisdiction and had actually argued, convincingly, that it was a corporate-creature under Texas law and thus properly before the federal judiciary.

This also addresses USAA's contention that its conduct in other cases cannot be used as a basis for sanctions in this case. USAA claims that because it properly asserted its unincorporated status in this case, it committed no sanctionable wrong. That contention rings hollow. USAA's error was in failing to provide this Court with the full exposition on the diversity question. Its error was in seeking to pretend that there was no authority of any other determination, despite the fact that USAA itself had

successfully argued that there was properly federal jurisdiction in another case. (See USAA's brief in *Pridgin v. USAA*, attached as Exhibit A.)

On the same grounds, this disposes of USAA's assertion that a sanction award in this case places it on the horns of a dilemma. It claims that, under the 10th Circuit's order in *Tuck v. USAA*, 859 F.2d 842 (10th Cir. 1988), it is required to withdraw from any federal case. If it does not do so, USAA contends, it is in violation of that court's order[1], but if it does do so, USAA contends, it may be subject to sanctions. WATERS does not contend that USAA must never bring a motion to dismiss when a federal case is filed against it. Rather, in filing such a motion, the issue should be presented, with a full disclosure of the situation and the conflicting rulings so that each individual court can examine the matter for purposes of its own jurisdictional determination.

More importantly, the cumulative misconduct present in this case is a factor which cannot be left unconsidered. USAA did not merely make its misrepresentation to one court and then mend its ways. It engaged in a deliberate manipulation of jurisdictional rules to suit its

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[1] Interestingly, it is only now, when USAA wants out of this federal court, that USAA is so concerned with not violating the 10th Circuit's admonition. USAA seemed unconcerned with violating the 10th Circuit's order when it continued to maintain its federal suit against the Hawaiian Insurance and Guaranty Co., Ltd. and lined its pocket with a $350,000 judgment in that case well over a year after the *Tuck* court's opinion was issued. (See Declaration and letter of Bill Souza, attached as Exhibit B.)

own purposes and needs. The government and the parties adverse to USAA each suffered losses due to that misconduct. That cumulative misconduct has not been brought home to USAA's doorstep. If USAA is permitted to escape liability for that conduct, what incentive is there for others to refrain from playing exactly the same jurisdictional game?

As noted by the Ninth Circuit in *Matter of Yagman*, 796 F.2d 1165, 1182:

> As judges, we are particularly sensitive to the problem of, and widespread concern over, frivolous litigation and the abusive practices of some attorneys. "These practices tend to impose unjustified burdens on other parties, frustrate those who seek to vindicate their rights in the courts, obstruct the judicial process, and bring the civil justice system into disrepute."

Additionally, the fact that the other cases cited in plaintiffs' opposing paper are suggested as the basis for assessment of damages is not improper. In *Yagman*, a police officer accused of causing the death of a jail prisoner sued the forensic pathologists involved in the case for defamation. The court held that the action was meritless and granted a directed verdict in favor of defendants. In addition, the trial court imposed $250,000 in sanctions against the plaintiff's attorney under FRCP 11 and 28 U.S.C. section 1927.[2] The appellate court noted that the

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[2] The fact that this was a Rule 11 case highlights how broadly the courts will reach to sanction abusive conduct. Although the language of Rule 11 and section 1927 narrowly circumscribe the circumstances under which sanctions may be

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trial judge's imposition of sanctions was for the trial counsel's cumulative conduct throughout the case. The appellate court expressed the concern that such a cumulative sanction at the *end* of the case defeated one of the primary purposes of sanctions: To deter future wrongful conduct. But the court also noted that:

> In some situations, liability under proper sanctioning authority will not be immediately apparent or may not be precisely and accurately discernible until a later time. For example, findings under Rule 11 occasionally cannot be made until after the evidentiary portion of the trial. A claim may appear to raise legitimate and genuine issues before trial, even in the face of summary judgment challenges, but will be unmasked as not well-founded in fact after the claimant has presented his evidence. And, in some cases, not until after the defendant's case-in-chief. The court must be able to respond to these situations with appropriate sanctions in the hope of deterring future inadequate filings by the certifying attorney and the trial bar in general. *Yagman, supra,* 796 F.2d at 1183.

That observation is particularly apt in this case. USAA's scheming could not have been immediately apparent to any of the other courts in which USAA practiced its manipulation. Rather, it was not until the

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awarded under those provisions, the courts still apply those provisions broadly in order to achieve the necessary salutory effect. Given that Rule 11 and section 1927 may be so broadly applied, it is certainly proper to give that same broad application to the court's inherent power.

cumulative effect could be discerned that USAA's conduct could be uncovered and addressed. As the *Yagman* court noted, the "court must be able to respond to these situations with appropriate sanctions in the hope of deterring future inadequate filings" by others. If USAA is permitted to escape unscathed in this case, as it did in the other 172 cases already documented, there will be no deterrent effect on USAA or on any other litigants from engaging in a similar practice. Indeed, if USAA is permitted to escape unscathed, it could encourage other exchanges, other associations and other attorneys and litigants to play the same game. However, if substantial sanctions are imposed on USAA, the news will spread through the legal community and, in future, other attorneys and litigants will take heed and take care that when they make jurisdictional allegations, those allegations are accurate and not misleading.

The existence of the other cases cited in plaintiffs' opposing papers not only provide evidence of USAA's wrongful conduct in this case, and so are relevant for consideration, their mere existence provides a proper factor in determining sanctions. In both *Freeze v. Griffith*, 849 F.2d 172 (5th Cir. 1988) and *Moody v. Miller*, 864 F.2d 1178 (5th Cir. 1989), the courts imposed sanctions on prisoners bringing civil rights violation cases against their wardens, noting that sanctions were proper given the numerous meritless cases previously brought by those same prisoners.

As noted by the Ninth Circuit is a Rule 11 case:

> If a court finds that a motion or paper, other than a complain, is filed in the context of *a*

> *persistent pattern of clearly abusive litigation activity*, it will be deemed to have been filed for an improper purpose and sanctionable. *Aetna Life Ins. Co. v. Alla Med. Serv. Co.*, 855 F.2d 1470, 1476 (9th Cir. 1988). (Emphasis added.)

USAA's chameleon-like character gave it an advantage over other litigants and over individual federal courts. Since objective evidence exists to prove that USAA has made use of this advantage, this Court need only ask if it will allow itself and other federal courts to be used as a vehicle for the frustration of meritorious claims. The "persistent pattern of clearly abusive litigation activity" evidenced by the Addendum is continuing in this case. Although USAA's motion to dismiss is not frivolous on its face, it was filed for the improper purpose of continuing the pattern of fraud USAA has so actively engaged in.

B. Although this case presents an unusual circumstance for imposition of sanctions, that fact should not permit USAA to escape the consequences of its jurisdictional scheming.

There is no dispute that this case presents a unique situation. That fact, however, should not preclude this Court's exercise of its power to punish for improper conduct. As noted by the *Yagman* court:

> Each case must be taken individually and evaluated in light of its own peculiar circumstances. If sanctions are warranted by those circumstances, the court should not waiver in imposing them. *Yagman, supra*, 796 F.2d at 1182.

If USAA is permitted to escape all punishment in this situation, the door will be open to others to conduct the same type of jurisdictional manipulation without fear of reprisal, even assuming it is ever discovered. Such conduct must be stopped and stopped now. As one court observed:

> Mounting federal caseloads and growing public dissatisfaction with the costs and delays of litigation have made it imperative that the federal courts impose sanctions on persons and firms that abuse their right of access to these courts. *Dreis & Krump, Inc. v. Intern. Ass'n of Machinists,* 802 F.2d 247, 255 (7th Cir. 1986).

USAA has repeatedly abused its right of access to the federal court system. Its conduct should not be swept under a rug and permitted to go unpunished or unchastised. An award of substantial sanctions is the only appropriate means for deterring this conduct by USAA or others.

C. The amount of sanctions should properly be based on the number of cases in which USAA exercised its jurisdictional game-playing.

Finally, the amount of sanctions to be awarded is a critical issue. As noted in the *Eash* case, the sanction award may properly include reimbursement to the government for the expenses it incurred as a result of a party's improper and bad faith conduct. Obviously, it would be a task of mind-boggling proportions to go back and examine every case and attempt to assess the precise amount of time, money and effort which was expended and wasted by each court when required to deal with

USAA's jurisdictional ploys. Suffice it to say that the judicial time wasted is of major proportions. Here we are not only talking about pleadings and motions, but entire trials that were unnecessary if USAA had not engaged in its nefarious conduct. It is fair to say that there were certainly between 50 and 100 cases where substantial judicial time was wasted. That does not even count the litigants' time and the attorneys' time that USAA required to be spent due to its wrongful conduct. Finally, there have been appeals that would not have been necessary and possibly decisions made which were based upon erroneous, misleading or incomplete information.

Indeed, this is a novel and unique situation. There has never before been disclosed such a widespread waste of judicial resources. As noted by one respected law professor who specializes in legal ethics in discussing this case, "[USAA] has manipulated its status so that no rule applies to it." (Stephen Gillers, as quoted in the *Los Angeles Times*, November 8, 1991, Metro Section, page B4, copy attached as Exhibit C.) Additionally, Jeffrey S. Brand, a federal litigation specialist and law professor at the University of San Francisco noted that this is the sort of situation that has prompted calls for reform of the nation's civil justice system and "conduct like this should be of great concern to everyone because it makes it impossible" for the legal system to function properly. (*Ibid.*)

The sanctions must be severe to get the proper message across. This is not an isolated event. This was a cold and calculated course of conduct over years which has just now been discovered and the wrongdoer is now simply being brought to account.

Due to the fact that the Government has suffered from the wasting of judicial resources at the hands of USAA, it is only proper that this Court consider awarding a portion of the sanctions to be paid to the U.S. Treasury. Naturally, the Waters should receive a portion of the sanctions award for their efforts in bringing the wrongdoer to account.

It is undoubtedly safe to assume that the proposed $10,000 per case figure (for a total of $1.7 million) would be a minimal amount expended by the judiciary and the Government as a result of USAA's misdeeds.[3] Plaintiff suggests that an award of sanctions be split between the U.S. Treasury and Plaintiff, or on some other formula basis so that the sanctions award makes sense both from a deterrence point of view and from the point of view of reimbursing the Government for the judicial time wasted over the past years. Although this is a unique and novel approach for the awarding of sanctions, this is in fact a unique and novel case. The integrity of the judicial process is at stake, and must be preserved. The Federal Courts must let parties know that those who attempt to tinker with the integrity of the judicial process on such a wide-scale basis, will find that the cost by way of sanctions will be high if their scheme is discovered. No other remedy make sense.

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[3] For example, in *Tuck* alone, the case went all the way through trial and judgment, was appealed once, USAA sought writ of certiorari to the United States Supreme Court, it was remanded back to the trial court for amendment of the complaint, the order on that amendment was appealed and the action settled only during the pendency of the *second* appeal.

Here, USAA does not disavow its conduct. It happened and it's a matter of record. They offer no apologies. Their only defense is that the Federal Court system has no power to punish them for their years of misconduct because it was only recently discovered. If that excuse succeeds, it will be a sad day for the judiciary.

D. Even if it is ultimately determined that this Court has no subject matter jurisdiction, it may still impose sanctions.

Even if it were ultimately determined by this honorable Court that subject matter jurisdiction does not exist, and cannot be conferred through amendment, this Court still has the power to levy sanctions. For example, in *Cooter & Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 S.Ct. 2447, 2455, ___ L.Ed.2d ___ (1990), the Supreme Court held that a district court could impose Rule 11 sanctions even after the plaintiff had dismissed the action. Similarly, in *Eash, supra*, 757 F.2d at 559-560, the court upheld the district court's power to impose sanctions even 11 days after dismissal of the case.

This is only logical. If a party attempts to abuse the federal jurisdictional process and then invokes the lack of subject matter jurisdiction in order to escape a sanction award for that conduct, the federal judiciary will be powerless to prevent exactly the abuses perpetrated by USAA. Thus, even if this action is dismissed, this honorable Court should exercise its inherent power to punish USAA for its conduct.

2.

UNDER TEXAS STATUTORY PROVISIONS, A RECIPROCAL INTERINSURANCE EXCHANGE SUCH AS USAA IS DEEMED TO BE A CORPORATION AND THE CORPORATION CITIZENSHIP RULES THUS APPLY TO THE JURISDICTIONAL DETERMINATION

Since the 1987 amendment to the Texas corporation statutes, it has been clear that, under Texas law, a reciprocal interinsurance exchange such as USAA is a corporation. Article 1302-1.03 of the Texas Miscellaneous Corporation Laws Act provides that the Texas Business Corporation Act shall govern all domestic corporations organized under any statute of the State. Tex. Rev. Civ. Stat. Ann. art. 1302-1.03 (Vernon Supp. 1991); *see also* Tex. Bus. Corp. Act, art. 9.14 (Vernon Supp. 1991) (making Act applicable to any domestic corporation organized under any state statute). As stated in Article 1302-7.06(A)(2) of the Texas Miscellaneous Corporation Laws Act:

> 'Corporation' means: (a) Any corporation, ***association,*** or other organization incorporated or ***organized*** under . . . ***the insurance Code*** . . .

Thus, under explicit Texas statutes, a reciprocal interinsurance exchange organized under Chapter 19 of the Texas Insurance Code, which USAA admits to being, is deemed to be a corporation under Texas law.

*Carden v. Arkoma Associates,* 494 U.S. 185, 110 S.Ct. 1015 (1990), relied on by USAA to argue that, as an unincorporated association, it is not subject to diversity jurisdiction in this case, decided only the very narrow question of whether the citizenship of only the general partners or both the general and limited partners in a

limited partnership are to be considered for determination of federal diversity jurisdiction. This Court is not dealing with a limited partnership and to that extent, the holding in *Carden* has no relevance. Beyond that, however, dicta in *Carden* actually supports the WATERS' position in this motion.

The dicta in *Carden* stands for the proposition that federal courts should not look beyond the issue of whether an entity is, or is not, a corporation under state law for purposes of the diversity determination. If a business entity has been organized under state law, and is defined under state law, as a corporation, then a corporation it is for diversity purposes. If it is not a corporation, *Carden* says the rules regarding association citizenship apply.

Texas deems reciprocal interinsurance exchanges to be corporations. For diversity purposes, federal courts are required, under *Carden* to follow this designation and treat a reciprocal exchange as a corporation – that is, a citizen of its state of organization and the state in which it locates its principal place of business. USAA, organized under the Texas Insurance Code and having its principal place of business in San Antonio, Texas, is a citizen of the state of Texas; therefore, there is complete diversity between the Waters and USAA.

In response to the Waters suit, USAA has cited *Baer v. USAA*, 503 F.2d 393 (2d Cir. 1974), which reads Texas Insurance Code Chapter 19 as treating reciprocal or interinsurance exchanges as unincorporated associations. USAA also cites *Tuck v. USAA*, 859 F.2d 842, 845 (10th Cir. 1988), where the Tenth Circuit felt constrained to simply

follow *Baer*'s holding that USAA was an unincorporated association, without any further analysis. However, the *Baer* court considered only a few sections of Chapter 19; nor did it look to Texas case law interpreting the chapter of the Insurance Code which provides for the establishment of reciprocal exchanges.[4] More importantly, since the Texas laws have changed since the *Baer* court made its determination, its holding has no further relevance to the issue.

Even if the statute itself were not enough, Texas case law also makes clear that reciprocal interinsurance exchanges are considered corporate entities for various purposes. For example, in *Kiepfer v. Beller,* the Fifth Circuit looked to the Texas Business Corporation Act to determine whether a director of a reciprocal insurance exchange was an agent of the exchange such that the exchange could be held liable for his actions. *Kiepfer v. Beller,* 944 F.2d 1213, 1217-18 (5th Cir. 1991) (citing Tex. Bus. Corp. Act, art. 9.14).

Long before this statutory definition of an exchange as a corporation was enacted, a Texas court of appeals

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[4] Indeed, as set forth in USAA's own brief in *Pridgin v. USAA,* United States District Court, Middle District of Georgia, Civil Action No. 84-247-ALB-AMER, a true and correct copy of which is attached as Exhibit A, USAA completely discredited the *Baer* decision and argued that it should be disregarded in federal diversity determinations. The fact that USAA disparaged *Baer* in one case, yet uses it in support of its position in this case, is yet another graphic example of USAA's penchant for talking out of both sides of its mouth and manipulating the law for its own purposes.

noted that in a reciprocal insurance exchange the subscribers were just like shareholders of a corporation in that their liability to pay their pro rata share of the losses took the place of the capital structure of a corporation. *Wilson v. Marshall,* 218 S.W.2d 345, 346 (Tex. Civ. App. – San Antonio 1949, no writ).

Article 19.03 of the Insurance Code provides that the declaration of the subscribers takes the place of Articles of Incorporation and that free surplus will constitute the capital structure of the exchange. Moreover, Article 19.13, added in 1987, makes the Texas Business Corporation Act relating to indemnification of officers and directors govern reciprocal or interinsurance exchanges.

This treatment of a reciprocal insurance exchange as a corporation comports with the way Congress has treated associations, specifically interinsurance exchanges, with regard to federal taxes and bankruptcy. In *Republic Underwriters v. Ford,* 100 F.2d 511, 514 (5th Cir. 1938), the Fifth Circuit held that the Texas state courts treated reciprocal exchanges like insurance companies, subject to applicable insurance laws; therefore, the Fifth Circuit held them to be insurance corporations under the bankruptcy law. The same is true under federal taxation law.

In *Kurzner v. United States,* 413 F.2d 97, 101-02 (5th Cir. 1969), the Fifth Circuit quoted a federal tax regulation which included in its definition of "association" an interinsurance exchange operating through an attorney-in-fact; however, as is still correct today, the IRS Code definition of "corporation" includes associations and insurance companies, but distinguishes partnerships and

trusts from corporations. 3A Z. Cavitch, *Business Organizations with Tax Planning*, sect. 64.02 (1991). The corporate characteristics which distinguish corporations from partnerships and trusts are as follows: (1) associates; (2) business purpose; (3) centralized management; (4) continuity of life; (5) limited liability; and (6) free transferability of interests. *Id.* Under the dictates of *Larsen v. Commissioner*, 66 T.C. 159 (1976), if an entity has more corporate characteristics than not, then it is a corporation as opposed to a partnership or trust, for federal tax purposes.

There are some Texas cases which have held that a reciprocal insurance exchange is not a corporation; but they predate the 1987 amendment to the Texas Miscellaneous Corporation Laws Act which defined as a corporation any association organized under the Insurance Code. Tex. Rev. Civ. Stat. Ann., art. 1302-7.06 (Vernon Supp. 1991). The court in *Hill v. Blanco National Bank*, 179 S.W.2d 999, 1005 (Tex. Civ. App. – Galveston 1944, writ ref'd w.o.m.), held that a reciprocal exchange was not a statutory entity. That simply is an incorrect statement of the law under the plain language of the statute and under subsequent case law interpretation. *Highway Insurance Underwriters v. Reed*, 221 S.W.2d 925, 926 (Tex. Civ. App. – Austin 1949, no writ), held that a reciprocal exchange was an association and not a corporation; however, in addition to the opinion's predating article 1302-7.06, the parties had also stipulated that the exchange was neither a corporation nor a partnership.

The Second Circuit in *Baer* premises its holding that a reciprocal exchange is an unincorporated association on the references in Insurance Code articles 19.03 and 19.06 to a stock insurance company – which the *Baer* court finds

must be different from a reciprocal exchange. The statute, however, never states that an exchange is an unincorporated association. Furthermore, the amendment of the article 1302-7.06 definition of "corporation" in 1987 overrides the *Baer* distinction.

Also in the 1987 amendments, the Texas legislature altered the provisions regarding service of process on an insurance company. Tex. Insur. Code Ann., art. 1.36 (Vernon Supp. 1991). Prior to that time, there was a separate provision for service on a reciprocal exchange. Tex. Insur. Code Ann. art. 19.04 (Vernon 1981) (repealed in 1987; see, now, art. 1.36). Under 1.36, all domestic insurance companies, including reciprocals, are to be served with process in the same manner – by serving the president, active vice-president, secretary, or attorney-in-fact at the home office or principal place of business of that carrier. Tex. Insur. Code Ann., art. 1.36, sect. 2a (Vernon Supp. 1991).

If the Texas legislature ever intended any distinction be made between a stock insurance company and a reciprocal insurance exchange, the 1987 amendments to the Insurance Code and the Texas Miscellaneous Corporation Laws Act obliterated that distinction. Since Texas statutory and case law clearly deem a reciprocal interinsurance exchange to be a corporation, and since, under *Carden*, no inquiry beyond that statutory designation is necessary or proper, it is manifestly clear that USAA is to be considered a corporation for purposes of the subject matter jurisdiction determination in this case.

3.

## DIVERSITY JURISDICTION MAY BE MAINTAINED BY ALLOWING AN AMENDED COMPLAINT WHICH NAMES DIVERSE SUBSCRIBERS OF UNITED SERVICES AUTOMOBILE ASSOCIATION AS REPRESENTATIVES OF A DEFENDANT CLASS.

It is abundantly clear that under *Carden* and under Texas law, USAA is a corporation for purposes of the jurisdictional determination to be made here. However, even if there was any doubt regarding USAA's corporate status, this Court would not be required to relinquish jurisdiction. Diversity jurisdiction could be maintained through the amendment of the original complaint. In the amendment plaintiffs would drop USAA as a party and name the Texas citizens that control us, as representatives of a defendant class consisting of USAA's many subscribers. Rule 23.2 of the Federal Rules of Civil Procedure authorizes such a class action.

Complete diversity of citizenship would exist under such an amendment because the Plaintiffs, as California domiciliaries, would be suing only the Texas individuals and corporations that actually run the business of USAA. Even though USAA claims over 180,000 California subscribers, the citizenship of these unnamed members of the defendant class is irrelevant to the existence of diversity jurisdiction. The Supreme Court initially announced this rule for determining citizenship in a class action in *Supreme Tribe of Ben-Hur v. Cauble,* 225 U.S. 356, 41 S.Ct. 338, 65 L.Ed. 673 (1921). Subsequently, the Court accepted without discussion the irrelevance of unnamed class members' citizenship in *Snyder v. Harris,* 394 U.S. 332, 340, 89 S.Ct. 1053, 1059, 22 L.Ed.2d 319 (1969).

The rule – considering only the citizenship of the named representatives – also has been applied in class actions brought pursuant to Rule 23.2. In *Kerney v. Fort Griffin Fandangle Association, Inc.*, 624 F.2d 717 (5th Cir. 1980), the plaintiff had unsuccessfully sought leave in the district court to amend his complaint to name, as a defendant class, the members of an association. The Fifth Circuit held that the plaintiff should have been allowed to amend and that his class action was authorized by Rule 23.2. 624 F.2d at 722. In addition, the court held that the plaintiff could satisfy the requirement of complete diversity by naming diverse representatives of the association and by dropping the association itself as a named party. 624 F.2d at 720. To the same effect is *Curley v. Brignoli, Curley & Roberts Associates*, 915 F.2d 81, 85 (2d Cir. 1990) *cert. denied*, ___, 111 S.Ct. 1430, 113 L.Ed.2d 484 (1991).

This Court has authority under Rule 15(a) of the Federal Rules of Civil Procedure to allow an amendment of the complaint to correct any jurisdictional flaws discovered in the original. Rule 15 states that leave of court "shall be freely given when justice so requires." Given the history of USAA's actions in federal court, it stands in an awkward position to claim that it would be prejudiced by such an amendment. Moreover, amendment of the complaint was strongly suggested as a jurisdictional cure for the difficulties caused by the same defendant in *Tuck v. United Services Automobile Association*, 859 F.2d 842, 846 (10th Cir. 1988).

Rule 23.2 of the Federal Rules of Civil Procedure expressly provides that an action may be maintained "against the members of an unincorporated association as

a class by naming certain members as representative parties." Those who promulgated the Rule (the Advisory Committee, the Supreme Court, and Congress) added only one limitation on the certification of such a class action – that it may proceed "only if it appears that the representative parties will fairly and adequately protect the interests of the association and its members."

Contrary to the plain language of Rule 23.2, some courts have engrafted a further limitation on the Rule. These courts have held that a Rule 23.2 class cannot be used in federal court where state law gives the unincorporated association capacity to sue or be sued in its own name – that is, where state law gives an unincorporated association jural status. See *Northbrook Excess and Surplus Insurance Company v. Medical Malpractice Joint Underwriting Association*, 900 F.2d 476, 478-79 (1st Cir. 1990); *Suchem, Inc. v. Central Aguirre Sugar Co*, 52 F.R.D. 348, 355 (D.P.R. 1971). *Patrician Towers Owners, Inc. v. Fairchild*, 513 F.2d 216 (4th Cir. 1975) was cited in *Northbrook* for this proposition as well, but the court in *Patrician Towers* noted but did not decide the issue. 513 F.2d at 220-21. In *Northbrook*, the First Circuit relied on the reasoning of *Suchem*, but the court in *Suchem* refused to allow a Rule 23.2 class both because the association had jural status and because the 11-member association did not satisfy the numerosity requirement of Rule 23(a). 52 F.R.D. at 352, 355.

Other courts have refused to create this "jural-status exception" to Rule 23.2. See *Curley v. Brignoli, Curley & Roberts Associates*, 915 F.2d 81, 87 (2d Cir. 1990), *cert. denied*, ___ U.S. ___, 111 S.Ct. 1430, 113 L.Ed.2d 484 (1991); *Kerney v. Fort Griffin Fandangle Association, Inc.*, 624 F.2d

717, 720 (5th Cir. 1980); *Lumbermen's Underwriting Alliance v. Mobil Oil Corporation*, 612 F. Supp. 1166, 1170 (D. Idaho 1985), aff'd 835 F.2d 1435 (1987).

In *Schiavone v. Fortune*, 477 U.S. 21, 106 S.Ct. 2379, 91 L.Ed.2d 18 (1986), the Supreme Court refused to accept an "identity-of-interest" exception to Rule 15(c) of the Federal Rules of Civil Procedure. The Court stated that the language of the Rule itself was central to the resolution of the issue. *Schiavone, supra*, 477 U.S. at 29, 106 S.Ct. at 2384. It went on to say that the choice was not between a liberal or a technical interpretation of Rule 15(c), but was, instead, a choice "between recognizing or ignoring what the Rule provides in plain language." The Court's choice was to "accept the Rule as meaning what it says." 477 U.S. at 30, 106 S.Ct. at 2384.

The plain language of Rule 23.2 does not support the creation of a jural-status exception. The Rule by its own language recognizes only one limitation – that the named representatives fully and fairly represent the interests of the association and its members. Since the drafters were able to write this limitation into Rule 23.2, one can conclude that they could have included a jural-status exception had such been intended.

Nevertheless, the First Circuit in *Northbrook* found support for its jural-status exception in the Advisory Committee Note to Rule 23.2. See 900 F.2d at 477. In the first sentence of the Note, the Advisory Committee observes that suits by or against representatives of an unincorporated association have often been viewed as class actions and that the "real or main purpose of this

characterization" was to grant entity status to associations that did not have jural status under Rule 17(b). From this comment, the *Northbrook* court concluded that the sole purpose of Rule 23.2 was to provide a class action only where state law did not give the association jural status. 900 F.2d at 478.

Although the Advisory Committee Note is to be given some weight in interpreting the Rule, we must here first interpret the Note. The more reasonable interpretation is that the drafters had concluded that, having proved valuable in overcoming the lack of an association's jural status, the class action device should be generally available. See *Curley v. Brignoli, Curley & Roberts Associates*, 915 F.2d 81, 87 (2d Cir. 1990), *cert. denied*, ___ U.S. ___, 111 S.Ct. 1430, 113 L.Ed.2d 484 (1991). If the drafters had in mind only the limited purpose ascribed to Rule 23.2 by the court in *Northbrook*, they could have more easily accomplished this result by extending to diversity cases Rule 17(b)'s grant of capacity to unincorporated associations in federal question cases. They could have thereby avoided drafting Rule 23.2 altogether. In the alternative, the drafters could have included the jural-status exception in the language of Rule 23.2, as noted above.

In the second sentence of the Advisory Committee Note to Rule 23.2, the drafters cite, as an example of their observation in the first sentence, the case of *Oskoian v. Canuel*, 269 F.2d 311 (1st Cir. 1959). *Oskoian* predated the adoption of Rule 23.2 and was a diversity case appealed from the United States District Court for the District of Rhode Island. The plaintiffs in *Oskoian* sought to sue a union by describing it as a defendant class under Rule 23.

Rhode Island law gave unincorporated associations entity status, 269 F.2d at 314, and allowed suit against their individual members, 269 F.2d at 314-15. The issue in the case, however, was whether the federal class action, which would be binding on the members of the union, could be maintained even though Rhode Island law prohibited such a binding class action. The court held that the Rule 23 class action could be maintained. 269 F.2d 316-17.

If the drafters had intended to restrict use of Rule 23.2 to those cases in which state law denied entity status to an unincorporated association, *Oskoian* would not have been cited as an example. The First Circuit in *Northbrook* observed that its earlier decision in *Oskoian* had no binding effect on the interpretation of Rule 23.2 because that decision predated the adoption in 1966 of Rule 23.2. *Northbrook*, 900 F.2d at 479. However, because of the citation of *Oskoian*, the Advisory Committee Note more clearly supports the proposition that Rule 23.2 applies even where state law grants entity status to unincorporated associations. See *Lumbermen's Underwriting Alliance v. Mobil Oil Corporation*, 612 F. Supp. 1166, 1170 (D. Idaho 1985), aff'd, 835 F.2d 1435 (1987); 7C C. Wright, A. Miller, & M. Kane, *Federal Practice and Procedure*, sec. 1861, at p. 223 (2d ed. 1986).

Another argument made for the restrictive approach to Rule 23.2 in *Northbrook* was that application of the Rule as it reads would allow the manufacture of diversity jurisdiction. See 900 F.2d at 478. However, even *Northbrook's* restrictive view allows a Rule 23.2 class in some cases. In these cases, therefore, diversity jurisdiction could be "manufactured" by naming class representatives

whose citizenship differs from that of the opposing parties. In reality, the undifferentiated concern for the protection of federal jurisdiction offers no special support for the argument that Rule 23.2 should be limited by a jural-status exception. Or, to put it another way, this undifferentiated concern could be used to justify any limit on a Federal Rule of Civil Procedure that had the effect of preventing the use of the Rule's procedural advantages to establish federal diversity jurisdiction.

Rule 23.2 is a purely procedural rule that allows the choice of certain named parties not unlike the choices available under Rules 20 and 23 of the Federal Rules of Civil Procedure. This procedural discretion necessarily carries with it the ability to name only diverse parties and thus to secure the benefits of a federal forum. No reason suggests itself for singling out Rule 23.2, rather than Rule 23 or Rule 20, for a restrictive reading simply because one of its advantages may be the maintenance of a diversity action. Although only indirectly related to this point, the Supreme Court has recently approved the decision of an appellate court to use Rule 21 in order to drop a non-diverse party so that diversity jurisdiction could be maintained for a judgment. *Newman-Green, Inc. v. Alfonzo-Larrain*, 490 U.S. 826, 109 S.Ct. 2218, 104 L.Ed.2d 893 (1989).

In *Suchem, Inc. v. Central Aguirre Sugar Co*, the district court held that a Rule 23.2 class action must satisfy the requirements of Rule 23(a) before it could be certified. 52 F.R.D. at 355. This restriction finds no support either in the language of Rule 23.2 or in its Advisory Committee Note. To the contrary, Rule 23.2 explicitly refers only to the provisions of Rule 23(d) and Rule 23(e), leaving one

to assume that the other parts of Rule 23 are inapplicable. Furthermore, the Advisory Committee Note to Rule 23.2 ends with the following sentence: "Ruled 23.2 deals separately with these actions, referring where appropriate to Rule 23." This language and the plain language of Rule 23.2 strongly suggest that the requirements of Rule 23(a) are not prerequisites to a Rule 23.2 class action. See *Curley v. Brignoli, Curley & Roberts Associates*, 915 F.2d 81, 86 (2d Cir. 1990), *cert. denied*, ___ U.S. ___, 111 S.Ct. 1430, 113 L.Ed.2d 484 (1991).

However, if this Court were to find that Rule 23(a) is applicable to a Rule 23.2 class action, the requirements of Rule 23(a) would be satisfied in this case. Often the most troublesome of Rule 23(a)'s prerequisites is the requirement of sufficient numerosity, but that requirement is obviously satisfied in this case since USAA has more than 180,000 subscribers in California alone. In fact, the very nature of this case proves the value of a Rule 23.2 or Rule 23 class action. The defendant class, made up of hundreds of thousands of individuals who are in reality only USAA's insurance clients, would be represented fairly and adequately by USAA's Texas attorney-in-fact and by the Texas corporations that make and implement USAA's business policies. These Texas citizens would, in any case, control the representation of USAA, and a class action frames this litigation in accordance with the real nature of this entity. Even though Texas law does not determine the applicability of Rule 23.2, it is suggestive to note that a reciprocal exchange can be sued as a defendant class in Texas courts. See *Richardson v. Kelly*, 191 S.W.2d 857, 860-61 (Tex. 1945), cert. denied, 329 U.S. 798, 67 S.Ct. 487, 91 L.Ed. 683 (1947).

A Rule 23.2 class action, naming as representative parties those who actually control USAA, is the most reasonable procedure for overcoming the rather preposterous legal fiction which appears to suggest that USAA is little more than an association of hundreds of thousands of equal partners.

## 4.

## CONCLUSION

Texas statutes and case law make it clear that USAA is deemed a corporation under Texas law. Accordingly, it should be treated as a corporation for purposes of diversity. Additionally, this Court would have jurisdiction pursuant to an amendment to the existing pleadings under Rule 23.2. For these reasons, this Court should retain jurisdiction of this matter.

There never has been a case where sanctions are more warranted to preserve the integrity of the judicial process. The federal court system itself has been a victim of USAA's jurisdictional manipulation resulting in countless hours, days, weeks and months of wasted judicial time. Likewise, litigants have paid money erroneously and attorneys have wasted valuable time. This has all resulted from USAA's wrongful conduct which has been perpetrated over a course of many years, demonstrating a pattern of abuse. It is important that this Court exercise its sound discretion, under its inherent power, to send the appropriate message in a way that makes sense from both the standpoint of reimbursing the government for its lost judicial resources as well as the important factor of deterrence. The fact that USAA offers no apologies for its

conduct is an aggravating circumstance that should be considered by this Court. USAA's argument that the federal courts have no power to sanction a litigant for years of abusing the federal process, simply because that conduct has been recently discovered, is a shallow argument which only suggests to any objective observer that USAA has no remorse for its actions.

Accordingly, a significant sanctions award is compelling.

Dated this 9th day of December, 1991 at Claremont, California.

Respectfully submitted,
SHERNOFF, BIDART & DARRAS

By: /s/
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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

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| LAUGHLIN E. WATERS AND VOULA WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | CASE NO: 91 3615 WFN (GHKx)<br><br>DECLARATION OF BILL SOUZA IN SUPPORT OF PLAINTIFFS' SUPPLEMENTAL BRIEFING AS ORDERED BY COURT IN OPPOSITION TO MOTION TO DISMISS AND IN SUPPORT OF REQUEST FOR SANCTIONS<br><br>[Judge Wm. Fremming Nielsen] |

Attached hereto is the Declaration of Bill Souza in support of plaintiffs' supplemental briefing as ordered by court in opposition to motion to dismiss and in support of request for sanctions.

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

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| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED STATES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. 91 3615 WFN<br><br>DECLARATION OF BILL SOUZA IN OPPOSITION TO MOTION TO DISMISS |

I, BILL SOUZA, DECLARE:

1. I am the Assistant Vice President and Claims Manager of Hawaiian Insurance and Guaranty Company, Ltd., ("HIG") a Hawaii Corporation. It is my responsibility to monitor claims litigation involving HIG. As a result, I am personally aware of and knowledgeable about the payment of the judgment in the action brought by United Services Automobile Association ("USAA")

against HIG, Case numbers CA No. 88-2941, CV-84-0300-ACK and CV-87-0483-ACK (consolidated).

2. As the result of the judgment in the action brought by USAA, HIG paid USAA the total amount of $391,343.50. That sum was paid in installments, the first in the amount of $353,417.88 on December 19, 1989, the second in the amount of $37,549.20 on March 8, 1990 and the third and final installment in the amount of $376.32 on April 13, 1990.

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct and that this declaration was executed on December 7th, 1991 at Honolulu, Hawaii.

/s/ Bill Souza
BILL SOUZA
Declarant

## PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On DEC. 10 1991, I served the foregoing document described as:

DECLARATION OF BILL SOUZA IN SUPPORT OF PLAINTIFFS' SUPPLEMENTAL BRIEFING AS ORDERED BY COURT IN OPPOSITION TO MOTION TO DISMISS AND IN SUPPORT OF REQUEST FOR SANCTIONS

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [X] a true copy

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>vs.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendants. | CASE NO. 91 3615 WFN<br><br>DEFENDANT'S SUPPLEMENTAL BRIEF IN SUPPORT OF MOTION TO DISMISS FOR LACK OF SUBJECT MATTER JURISDICTION AND IN OPPOSITION TO REQUEST FOR SANCTIONS<br><br>(Judge Wm. Fremming Nielson)<br><br>Trial Date: March 3, 1992 |

COMES NOW Defendant UNITED SERVICES AUTOMOBILE ASSOCIATION ("USAA") and, pursuant to the

Court's direction, submits its Supplemental Brief In Support of Motion To Dismiss For Lack Of Subject Matter Jurisdiction And In Opposition To Request For Sanctions as follows.

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

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|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS, Plaintiffs, vs. UNITED STATES AUTOMOBILE ASSOCIATION, Defendants. | CASE NO. 91 3615 WFN<br>DEFENDANT'S SUPPLEMENTAL BRIEF IN SUPPORT OF MOTION TO DISMISS FOR LACK OF SUBJECT MATTER JURISDICTION AND IN OPPOSITION TO REQUEST FOR SANCTIONS<br>(Judge Wm. Fremming Nielson)<br>Trial Date: March 3, 1992 |

## INTRODUCTION

In their supplemental brief, Plaintiffs LAUGHLIN E. WATERS and VOULA D. WATERS appear to agree with USAA: (1) that this Court lacks subject matter jurisdiction under the Supreme Court's decision in *Carden v. Arkoma Assocs.*, 494 U.S. 185 (1990), unless USAA is a corporation under Texas law (Supp. Br. 18-19); (2) that sanctions cannot be awarded unless USAA acted improperly in this action (Supp. Br. 6, 8-9); and (3) that it is proper for "USAA [to] bring a motion to dismiss when a federal case is filed against it" (Supp. Br. 9).

Plaintiffs nonetheless argue that maintenance of this action in federal court is permissible and that sanctions are appropriate. Plaintiffs are wrong. First, under Texas law, USAA is a reciprocal insurance exchange – an artificial entity that, as a matter of statute, is distinct from a corporation. The Texas statute from which Plaintiffs selectively quote (Supp. Br. 18) does not support a contrary result.

Second, contrary to Plaintiffs' suggestions (Supp. Br. 6,8), there is no basis for sanctioning USAA for failing to apprise the Court of the argument that USAA is a corporation or should be treated "like" a corporation. As noted, USAA is a reciprocal insurance exchange, which Texas law makes clear is a type of unincorporated association, not a corporation. In addition, the United States Supreme Court's decision in *Carden* foreclosed the argument that a non-corporate entity can be treated "like" a corporation for diversity purposes. Thus, USAA cannot conceivably be sanctioned for failing to advise the court of these arguments. In any event, USAA did advise this Court of

the Tenth Circuit's decision in *Tuck v. USAA*, 859 F.2d 842 (10th Cir. 1988), *cert. denied*, 489 U.S. 1080 (1989), which described the history of USAA's federal diversity litigation.

Finally, Plaintiffs err in suggesting (Supp. Br. 24-33) that, even if this Court lacks subject matter jurisdiction, they should be permitted to amend their complaint to restructure this suit as a class action against USAA's individual members. Such a step is legally impermissible.

While USAA believes that Plaintiffs' arguments are meritless, it wishes to assure this Court that it takes seriously its obligation to avoid appearing in federal court in diversity cases and acknowledges that its past record in this regard has been flawed. A number of factors no doubt contributed to this situation. USAA's jurisdictional status as a reciprocal insurance exchange makes it unique among the country's largest insurers. USAA utilizes over 3000 outside counsel to manage its large (over 15,000 case) litigation docket, and gives these outside counsel considerable autonomy in handling individual cases. These local counsel (most of whom routinely handle litigation for other insurers in federal court) were not always familiar with USAA's non-corporate status. Even within USAA, litigation is managed on a very decentralized basis, with regional claims personnel and file handlers having primary responsibility for monitoring ongoing litigation.

Following the decision in *Carden* and *Tuck*, USAA has moved to implement a litigation policy consistent with the principles laid down in those cases. For example, USAA sent an internal memorandum to all of its senior

claims attorneys, claims attorneys, litigation supervisors, and casualty file handlers advising them of the situation and instructing them that "USAA should appear neither as a plaintiff nor defendant" in diversity actions; sent a memorandum to over 3200 outside counsel directing them to refrain from litigating in federal court; and prepared a special litigation manual for outside counsel that highlighted the jurisdictional issue. USAA also has determined to conduct annual reviews to remind claims personnel and outside counsel of this policy and to annually monitor compliance. USAA's actions in this case are part of this established policy to comply with *Carden* and *Tuck*.

## ARGUMENT

### I. USAA Is a Reciprocal Insurance Exchange, Which Under Texas Law Is Considered To Be An Unincorporated Association Rather Than A Corporation

The resolution of USAA's motion to dismiss for lack of subject matter jurisdiction is controlled by the Supreme Court's 1990 *Carden* decision. In *Carden*, the Court addressed the proper status of a limited partnership for diversity purposes. The Court noted that the "[t]he precise question posed under the terms of the diversity statute is whether [the] entity may be considered a 'citizen' of the State under whose laws it was created." 494 U.S. at 187. While corporations had long been considered to be citizens of their States of incorporation, the *Carden* Court announced that it would "firmly resist[] extending that treatment to other entities." *Id.* at 189. Rather, for the "wide assortment of artificial entities" that "[t]he 50 States have created, and will continued[sic] to create," the

Court held that their citizenship must be measured by the citizenship of each of their members:

> In sum, we reject the contention that to determine, for diversity purposes, the citizenship of an artificial entity, the court may consult the citizenship of less than all of the entity's members. . . . [Rather,] a suit by or against the entity depends on the citizenship of all the members.

*Id.* at 195-97 (quotation omitted). Thus, under *Carden*, the question is not precisely what type of artificial entity USAA is, but whether USAA is considered to be a corporation under Texas law. A review of the relevant Texas statutes and cases makes clear that it is not; USAA is a reciprocal insurance exchange, a particular type of artificial entity created by the Texas Insurance Code that is distinct from a corporation and that is most accurately characterized as an unincorporated association.

### A. Texas Law Establishes Reciprocal Insurance Exchanges as Distinct Statutory Entities

A reciprocal insurance exchange is a type of insurance organization that is recognized in most states, and that can be generally defined as "an association of individuals or juristic entities, providing insurance among themselves and operating through a person or corporation that serves as attorney-in-fact." R. Keeton, *Insurance Law* 21 (1971).[1] In Texas, reciprocals are regulated by a

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[1] *See also* 18 J. Appleman, *Insurance Law & Practice* § 10121, at 224 (1945) ("A reciprocal or interinsurance 'exchange' is an

(Continued on following page)

special chapter of the Texas Insurance Code, Chapter 19. This Chapter provides the basic "authori[ty] to exchange reciprocal or interinsurance contract." Tex. Rev. Civ. Stat. Ann. art. 19.01. Under this arrangement, an individual subscriber is both an insurer and an insured, paying in premiums that are pooled with other premiums to create a fund to pay losses incurred by the reciprocal's subscribers. *Id.* art. 19.01. Each subscriber appoints an "attorney in fact" to issue the insurance contracts and to conduct the "business of the exchange." *Id.*, art. 19.02.[2]

Texas law is careful to establish reciprocal exchanges as particularized entities, distinct from regular insurance corporations. The statute expressly directs that "[t]he office or offices through which such indemnity contracts shall be exchanged shall be classified as reciprocal or interinsurance exchanges." Tex. Rev. Civ. Stat. Ann. art.

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association of persons cooperating through an attorney in fact for the purpose of insuring themselves and each other. Such insurance has been held distinguishable from all other forms of insurance, in that every insured is an interinsurer, and every insurer is an insured.") (footnotes omitted).

[2] The attorney in fact is required to file a "declaration of subscribers" with the Texas Board of Insurance Commissioners. Tex. Rev. Civ. Stat. Ann. art. 19.03. This declaration must set forth the "name or title of the office at which subscribers propose to exchange . . . indemnity contracts"; the "kind or kinds of insurance to be . . . exchanged"; and"[t]he location of the office or offices from which such contracts or agreements are to be issued." *Id.* The attorney in fact also is required to obtain a certificate of authority from the Commissioner, which licenses him and authorizes him to conduct the business of the reciprocal exchange. *Id.*, art. 19.10.

19.03(1). Likewise, the Insurance Code definition of "person" includes various types of entities, but specifically distinguishes "reciprocal exchanges" from "corporations": "person [means] any individual, *corporation*, association, partnership, *reciprocal exchange*, interinsurer, Lloyds insurer, fraternal benefit society, and any other legal entity engaged in the business of insurance." *Id.*, art. 21.21(2)(a) (emphasis added). Indeed, the Insurance Code Chapter establishing reciprocal exchanges expressly distinguishes these entities from corporations by specifying that a reciprocal exchange can limit its subscribers' contingent liabilities "if the free surplus [of the reciprocal] is equal to the minimum capital stock and minimum surplus required of a stock company transacting the same kinds of business." *Id.*, art. 19.03(3).[3] Any possible doubt concerning the distinctive nature of reciprocal exchanges is removed by the final article of the Chapter on reciprocal exchanges, which provides that "[r]eciprocal or intrinsurance exchanges shall be exempt from the operation of all insurance laws of this State except as in this Chapter specifically provided, or *unless reciprocal or interinsurance exchanges are specifically mentioned in such other laws.*" *Id.*, art. 19.12 (emphasis added).

This distinction between reciprocal exchanges and corporations is preserved throughout the Insurance Code. Reciprocals are subject to some of the same general regulatory requirements as other types of insurers, including

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[3] "Free surplus" is the amount by which a reciprocal exchange's assets exceed its liabilities, including reserves. *See Archie v. Knox*, 224 S.W.2d 504, 506 (Tex. Civ. App. – Austin 1949, writ ref'd n.r.e.).

corporations, but the statute acknowledges the different nature and structure of reciprocal exchanges. For example, while corporations must submit their "articles of incorporation" to the Board of Insurance Commissioners, and must have their "proposed capital structure" analyzed by the Board in order to qualify to conduct insurance business, the Code recognizes that reciprocal exchanges as unincorporated entities, will have neither "articles of incorporation" nor a "capital structure." Tex. Rev. Civ. Stat. Ann. arts. 2.01, 2.04. Rather, the Insurance Code provides that, for reciprocals, the "declaration of subscribers shall be in lieu of Articles of Incorporation," and "[f]ree surplus shall constitute capital structure." *Id.*, art. 19.03(5). This distinction between corporations and reciprocal exchanges is reiterated in the Insurance Code's specification that an insurer is considered insolvent and must cease to do business in Texas when its surplus is "impaired to the extent of more than fifty (50%) per cent of [the] required minimum surplus of a capital stock insurance company, *or in case . . . the minimum surplus of a reciprocal* . . . [is] impaired to the extent of more than sixteen and twothirds[sic] (16 2/3%) per cent of [the] required minimum surplus." Tex. Rev. Civ. Stat. Ann. art. 1.10(5) (emphasis added).[4] These deliberate references

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[4] Similarly, this same article distinguishes corporations from reciprocals in giving the Board of Insurance Commissioners power to sanction "domestic and foreign, stock and mutual life, health, and accident *insurance companies*; domestic and foreign, stock and mutual, fire and casualty *insurance companies*; Mexican casualty insurance companies; domestic and foreign Lloyd's plan insurers; [and] domestic and foreign *reciprocal or interinsurance exchanges*. . . . " Tex. Rev. Civ. Stat. Ann. art. 1.10(7)(h) (emphasis added).

throughout the Insurance Code make clear that reciprocal exchanges are regarded by Texas law as distinct entities, and are not corporations. Rather, reciprocal exchanges are generally regarded as unincorporated associations. *See, e.g., Baer v. USAA*, 503 F.2d 393, 394 (2d Cir. 1974) (noting that "an 'interinsurance exchange' or 'reciprocal insurance association,' both . . . are familiar types of unincorporated associations").[5]

Indeed, it is impossible to consider reciprocal exchange to be a corporation in light of the provisions of the Texas Business Corporation Act. Under Texas law, "a corporation is distinguishable from a mere aggregation of individuals associated for a common purpose in that, even though the latter may be recognized by the law as a unity for purposes of suit, the full import of the term 'corporate entity' is lacking." 15 Tex. Jur. 3d *Corporations* § 1, at 135 (1981) (footnotes omitted). To qualify as a "corporate entity" under Texas law, the entity must have been formed pursuant to the Business Corporation Act. *See* Tex. Bus. Corp. Act art. 1.02. Under the Act, incorporators must prepare articles of incorporation (*id.*, art. 3.01), which must include 13 specific elements (*id.*, art.

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[5] *Accord, e.g.*, 46 C.J.S. *Insurance* § 1412(b), at 734 ("A reciprocal or interinsurance exchange is something more than a partnership and something less than an insurance corporation and falls within the classification of unincorporated companies."); 43 Am. Jur. 2d *Insurance* § 77, at 157 ("reciprocal associations or exchanges have no corporate existence"); *see also* R. Keeton, *Insurance Law* at 21; 18 J. Appleman, *Insurance Law and Practice* § 10121.

3.02),[6] and then must file those articles with the Texas Secretary of State (*id.*, art. 3.03). Only after articles of incorporation are filed does Texas issue a certificate of incorporation designating the artificial entity as a corporation. *Id.*, art. 3.03. USAA, as a reciprocal exchange, has taken none of these steps and thus cannot be regarded as a corporation under the Texas statutes.

Texas case law confirms the distinctive status of a reciprocal exchange. Even Plaintiffs recognize (Supp. 22) that "Texas cases . . . have held that a reciprocal insurance exchange is not a corporation." For example, in *Highway Ins. Underwriters v. Reed*, 221 S.W.2d 925 (Tex. Civ. App. – Austin 1949, no writ), the trial court had held that the defendant, " 'a reciprocal insurance exchange, was and is an 'association' ' for venue purposes. *Id.* at 926 (quoting trial court finding of Fact). The *Reed* Court affirmed, expressly holding that the reciprocal exchange "is an association [for purposes of the venue statute] . . . not a corporation or partnership." *Id.* at 927; *see also Howell v. Knox*, 211 S.W.2d 324, 326-27 (Tex. Civ. App. – Austin 1948, writ ref'd. n.r.e.) (noting that "[t]he reciprocal or interinsurance exchange is a creature of the statutes . . . and its powers, duties, responsibilities and methods

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[6] These elements that must be covered in articles of incorporation include items that clearly are inapplicable to a reciprocal exchange, such as "[t]he aggregate number of shares which the corporation shall have authority to issue," the par value of each of such shares," and the existence of "[a]ny provision limiting or denying to shareholders the preemptive right to acquire additional or treasury shares of the corporation." Tex. Bus. Corp. Act. arts. 3.02(4), (8).

of operation are regulated by statute") (quotations omitted); *Mercer v. Knox*, 192 S.W.2d 884 (Tex. Civ. App. – Austin 1946) (same); *Baer v. USAA*, 503 F.2d at 394-95 (reviewing Texas statutes on reciprocal exchanges). Thus, a reciprocal exchange has been recognized as occupying a unique role under Texas law, with a distinct statutory origin.[7]

Plaintiffs cite no Texas case indicating reciprocal exchanges are corporations under Texas law; instead, they point (Supp. Br. 20-22 (emphasis added)) to several federal court cases suggesting "reciprocal interinsurance exchanges are *considered* corporate entities *for various purposes*."[8] For example, Plaintiffs cite (Supp. Br. 20) *Kiepfer v. Beller*, 944 F.2d 1213 (5th Cir. 1991), in which the Fifth

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[7] Case law from other jurisdictions also recognizes the distinctive nature of a reciprocal exchange as a statutory entity that is considered to be an unincorporated association, not a corporation. *See Casualty Reciprocal Exchange v. Compton*, 633 S.W.2d 463, 464 (Mo. App. 1982) ("[A] reciprocal or interinsurance exchange is something more than a partnership and something less than an insurance corporation, and falls within the classification of unincorporated companies.") (quotations omitted); *See also, e.g., Automobile Club Inter-Insurance Exchange v. Gaertner*, 636 S.W.2d 68, 71 (Mo. 1982) (en banc); *Citizens Automobile Inter-Insurance Exchange v. Andrus*, 70 Idaho 114,212 P.2d 406 (1949);*Industrial Indem. Exchange v. State Bd. of Equalization*, 26 Cal.2d 772, 161 P.2d 222 (1945); *In re Int'l Re-Insurance Corp.*, 32 Del. Ch. 471, 86 A.2d 647 (1952); *Farmers Automobile Inter-Insurance Exchange v. MacDonald*, 59 Wyo. 352, 140 P.2d 905 (1943).

[8] The only Texas case Plaintiffs city (Supp. Br. 21) is *Wilson v. Marshall*, 218 S.W.2d 345 (Tex. Civ. App. – San Antonio 1949, no writ), but their attempt to find support in that case is

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Circuit determined whether a reciprocal exchange's director was acting as an agent of the exchange by considering the general provisions of the Texas Business corporation Act. But in looking to the Business Corporation Act for this limited purpose, *Kiepfer* did not suggest that the Act was generally applicable to reciprocal exchanges. Instead, the Court made clear that it did so only bec10use[sic] the Insurance Code contained no provision dealing with the agency issue, and "[w]hen the Insurance Code fails to address some question of corporate law, it is supplemented by the provisions of the Texas Business Corporation Act to the extent that the Business corporation Act is consistent with the Insurance Code." *Id.* at 1218 n.1 (citing Tex. Bus. Corp. Act art. 9.14).[9] *Kiepfer* therefore does not address the proper characterization of a reciprocal exchange for diversity purposes.[10] Left with no genuine

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unavailing. In *Wilson*, the court noted that subscribers to a reciprocal exchange are the "owners" and thus "stand[] in the position of a stockholder in a stock insurance company." *Id.* at 346. Thus, *Wilson* plainly recognized that the two types of entities are distinct, and merely observed that there was a similarity in one respect.

[9] It clearly would not be "consistent" to read the business Corporation Act to override the Insurance Code's careful distinction between reciprocal exchanges and corporations.

[10] Likewise, Plaintiffs' attempt (Supp. Br. 21-22) to find support in cases applying federal bankruptcy statutes or federal tax regulations is misplaced. *Republic Underwriters v. Ford*, 100 F.2d 511 (5th Cir. 1938), deals with the proper interpretation of federal bankruptcy laws. Moreover, as one of Plaintiffs' own cases (Supp. Br. 21 notes, "an entity may be a corporation for federal tax purposes even though it is something less under

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case authority, Plaintiffs attempt to distinguish the Texas cases by claiming they are no longer good law in light of a 1987 amendment to the Texas Miscellaneous Corporation Laws Act.

B. Plaintiffs' Effort to Rely On A 1987 Statute To Characterize Reciprocal Exchanges As Corporations Is Unfounded.

There is no support for Plaintiffs' suggestion (Supp. Br. 18-24) that this 1987 amendment to the Texas Miscellaneous Business Corporation changed the legal status of reciprocal exchanges under Texas law from unincorporated associations to corporations. The provision they cite, Article 1302-7.06(A)(2), does provide a definition or "corporation," *but that definition is for the limited purpose of authorizing Texas entities to eliminate their directors' liability for actions undertaken in good faith.* In claiming it has broader applicability, Plaintiffs have misquoted and fundamentally misread the statue.

The limited purpose of Article 1302-7.06(A)(2) is made clear in the very title of the Act; this provision was enacted in 1987 as "An Act relating to liability of certain directors of certain corporations and associations." Acts 1987, 70th Leg., ch. 424 *cited in* Tex. Rev. Civ. Stat. Ann.

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state law." *Kurzner v. United States*, 413 F.2d 97, 104 (5th Cir. 1969). Thus, federal bankruptcy or tax law hardly shed light on the proper categorization of a reciprocal exchange under Texas state law.

§ 1302-7.06, Title of Act (Vernon Supp. 1991).[11] Likewise, the text of the statute, which Plaintiffs quote in an incomplete fashion, makes it clear that the definition does not have the broad applicability they suggest. Specifically, part A of the article provides that:

> A. *In this article*: . . .
>
> (2) "Corporation" means:
>
> (a) Any corporation, association, or other organization incorporated or organized under the Texas Business Corporation Act, the Texas Nonprofit Corporation Act . . . , The Texas Banking Code of 1943 . . . , the Insurance Code . . . , the Texas Savings and Loan Act . . . , the Texas Credit Union Act . . . , the Cooperative Association Act . . . , The State Housing Law . . . , the Electric Cooperative Corporation Act . . . , the Telephone Cooperative Act . . . , The Texas Professional Association Act . . . , the Texas Mutual Trust Investment Company Act . . . , the Health Facilities Development Act . . . , the Texas Transportation Corporation Act . . . , the Cultural Education Facilities Corporation Act . . . , the Hospital Authority Act . . . , or the Higher Education Authority Act. . . .

Tex. Rev. Civ. Stat. Ann. art. 1302-7.06(A)(2) (citations and references to some Acts omitted; emphasis added). Plaintiffs' quotation of this provision (Supp. Br. 18) inexplicably omits the highlighted introductory clause, which

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[11] *Accord, e.g.*, Chadwick, *Corporations and Partnerships*, 42 Sw. L.J. 249, 266 (1988) (noting purposes of Article 1302-7.06) was to "encorage qualified persons to serve as directors by reducing their exposure to liability").

emphasizes the definition's limited scope. It is only this omission that allows Plaintiffs to argue that the definition renders a reciprocal exchange a corporation for all purposes under Texas law.[12]

Indeed, Plaintiffs' reading of Article 1302-7.06(A)(2) would not only turn reciprocal exchanges into corporations for all purposes, but would convert a wide variety of other unincorporated entities into corporations as well. For example, entities organized under the Texas Professional Association Act fall within the scope of Article 1302-7.06(A)(2), and thus, under Plaintiffs' reasoning, would be considered corporations. Yet the Texas Professional Association Act itself makes clear that the artificial entity it establishes is "a professional association, *as distinguished from* either a partnership or *a corporation*." Tex Rev. Civ. Stat. Ann. art. 1528f(2) (emphasis added). In short, Plaintiffs have sought to place more weight on Article 1302-7.06 than that limited provision can possibly bear, and their argument therefore collapses.

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[12] Not only does the introductory clause clearly limit the reach of the definition, but the other portions of Article 1302-7.06 also indicate that the definition sweeps in entities that are generally not considered to be corporations. Thus, for example, subsections (A)(1) includes within the definition of "articles of incorporation" "any other document required to incorporate or organize" one of the specified entities, and "director" is defined to include an individual serving as a "trustee." *Id.*, arts. 1302-7.06(A)(1), (3).

II. There Is No Factual Or Legal Basis For Sanctions Against USAA

USAA's conduct in this case has followed precisely the course of action mandated by the Supreme Court's decision in *Carden* and by the Tenth Circuit's decision in *Tuck*. The complaint in this action was filed on July 5, 1991. Given *Carden's* recent clarification that the citizenship of an artificial entity other than a corporation is determined, for diversity purposes, by reference to the citizenship of each of the entity's members (494 U.S. at 195-96), and given the Tenth Circuit's express directive to USAA to "make . . . motions [to dismiss] in all pending diversity litigation" (859 F.2d at 845 n.3), USAA took the only possible step – it filed its motion to dismiss for lack of subject matter jurisdiction. In its supporting papers, USAA directed the Court's attention to *Tuck*, where the issue of USAA's jurisdictional status and history of litigation in federal court is fully discussed. Thus, USAA's actions were entirely proper and did not constitute the type of abusive, frivolous, or bad faith litigation tactics that warrant sanctions.

In their initial request for sanctions, Plaintiffs suggested (Mem. 26-30) that USAA should be sanctioned here for its conduct in other cases, whether or not USAA had engaged in any misconduct in this case USAA's reply pointed out that Rule 11 does not allow the imposition of sanctions for allegedly wrongful conduct in other cases where no misconduct had occurred in the case before the court. *See Soules v. Kauaians for Nukolii Campaign Comm.*, 849 F.2d 1176, 1185 (9th Cir. 1988); *Burull v. First Nat'l Bank of Minneapolis*, 831 F.2d 788, 790 (8th Cir. 1987), *cert.*

*denied*, 485 U.S. 961 (1988); ABA *Standards and Guidelines for Practice Under Rule 11 of the Federal Rules of Civil Procedure*, 121 F.R.D. 101, 111 (1988). Plaintiffs cite no cases, involving either Rule 11 or the courts' inherent authority, that in any way suggest the contrary. Instead, in their supplemental brief, Plaintiffs have changed course, and now argue that sanctions amounting to approximately $1.7 million should be imposed solely because USAA, in its motion to dismiss, did not inform this Court that it had previously taken the position in other cases that it could be characterized as a citizen of Texas for diversity purposes. *See* Supp. Br. 6, 8-9. Plaintiffs' attempt to predicate an unprecedented sanctions award on this alleged failure to cite contrary authority is without support.

*First*, there is no obligation to include legally incorrect arguments in a pleading filed with this Court. As discussed above (*supra* pp. 5-13), there is no support for the argument that USAA is a corporation under Texas law. Likewise, there is no support for the argument that USAA should be treated "like" a corporation for diversity purposes; indeed, the Supreme Court's recent decision in *Carden* plainly forecloses any such argument.

Plaintiffs suggest (Supp. Br. 8) that USAA should have presented here the arguments it made in *Pridgin v. USAA*, No. 84-247-ALB-AMER (M.D. Ga. filed Nov. 14, 1984), and go so far as to attach USAA'S memorandum in that case to their supplemental brief. In *Pridgin*, USAA removed the case to federal court, and after the plaintiff

moved for remand on the basis of *Baer*, 503 F.2d 393,[13] USAA argued that *Baer* was distinguishable and that the federal court could properly exercise diversity jurisdiction. USAA based its argument primarily on two Supreme Court cases – *Puerto Rico v. Russell & Co.*, 288 U.S. 476 (1933), and *Navarro Savings Ass'n v. Lee*, 46 U.S. 458 (1980) – and on the fact that in the 10 years since *Bear*, it had as a practical matter grown to the point that it operated more like a corporation. *See* Supp. Br., Ex. A at 36-39, 42-43.

In asserting (Supp. Br. 8) that it was error for USAA not to make these same arguments here, Plaintiffs overlook the controlling fact that the Supreme Court in *Carden* expressly and definitively rejected each of the arguments that USAA had made in *Pridgin*. *Carden* ruled that neither *Puerto Rico v. Russell & Co.* nor *Navarro Savings* created exceptions to the rule that the citizenship of an artificial entity for diversity purposes is determined by reference to all of the entity's members. *See* 494 U.S. at 189-92. Similarly, *Carden* expressly rejected the argument, like that made by USAA in *Pridgin*, that "business reality . . . should be taken into account for purposes of determining whether an artificial entity is a citizen." *Id.* at 192. Thus, the arguments made in *Pridgin* were considered and rejected by the Supreme Court. By claiming that USAA nonetheless should be sanctioned, Plaintiffs are making the remarkable suggestion (Supp. Br. 8) that, to

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[13] In *Baer*, the Second Circuit held that USAA was an unincorporated association and should be considered, for diversity purposes, to be a citizen of each state in which it has members. *See* 503 F.2d at 395-96.

avoid sanctions, a litigant must discuss contrary arguments that have been definitively rejected.

The Ninth Circuit already has rejected this standard as a basis for sanctions. In *Golden Eagle Distributing Corp. v. Burroughs Corp.*, 801 F.2d 1531, 1542 (9th Cir. 1986), the court held that:

> neither Rule 11 nor any other rule imposes a requirement that the lawyer, in addition to advocating the cause of his client, step first into the shoes of opposing counsel to find all potentially contrary authority, and finally into the robes of the judge to decide whether the authority is indeed contrary or whether it is distinguishable. It is not in the nature of our adversary system to require lawyers to demonstrate to the court that they have exhausted every theory, both for and against their client.

*See also Townsend v. Holman Consulting Corp.*, 929 F.2d 1358, 1363 (9th Cir. 1990) (en banc); *United States v. Stringfellow*, 911 F.2d 225, 226 (9th Cir. 1990); *Mercury Serv., Inc. v. Allied Bank of Texas*, 117 F.R.D. 147, 157 (C.D. Cal. 1987), *aff'd mem.*, 907 F.2d 154 (9th Cir. 1990). Plaintiffs cite nothing to the contrary; indeed, none of the sanctions cases Plaintiffs cite involve an alleged failure to disclose contrary authority, and simply have nothing to do with the situation presented here. For example, Plaintiffs devote considerable space to discussing (Supp. Br. 9-12) *In re Yagman*, 796 F.2d 1165 (9th Cir. 1986), *cert. denied*, 484 U.S. 963 (1987), *Freeze v. Griffith*, 849 F.2d 172 (5th Cir. 1988), and *Moody v. Miller*, 864 F.2d 1178 (5th Cir. 1989). But these cases offer Plaintiffs no support. In *Yagman*, the trial court imposed sanctions on plaintiffs' counsel for filing a complaint the trial judge deemed frivolous and

for certain discovery abuses. *See* 796 F.2d at 1182, 1186-87. *Yagman* not only thus has no bearing here, but more important, Plaintiffs completely ignore the fact that the Ninth Circuit reversed and held that imposition of sanctions was improper. *Id.* at 1188. *Freeze v. Griffith* is similarly inapposite; it involved the imposition of costs on a pro se prisoner by an appellate court pursuant to 28 U.S.C. § 1915(e),[14] for filing a frivolous appeal. *See* 849 F.2d at 176. Plaintiffs' reference (Supp. Br. 12) to *Moody v. Miller* also does not support their position. In that case, the district court dismissed a pro se prisoner's lawsuit as frivolous and imposed sanctions for court costs. 864 F.2d at 1179.

Finally, *In re Ronco, Inc.*, 838 F.2d 212 (7th Cir. 1988) (cited at Supp. Br. 6-7), also is irrelevant here. In *Ronco*, the court sanctioned counsel for arguing for a continuance on the ground that he had had inadequate time to analyze the legal issue involved due to his very recent appointment as special counsel for a creditors' committee in a bankruptcy proceeding. In fact, however, the attorney had spent considerable time on that exact issue prior to his appointment through his representation of an individual creditor in the same bankruptcy proceeding. This type of nondisclosure is tantamount to an affirmative misrepresentation, and obviously bears no resemblance to the nondisclosure of contrary authority that Plaintiffs

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[14] Section 1915(e) provides, in relevant part, that in an in forma pauperis proceeding, "[j]udgment may be rendered for costs at the conclusion of the suit."

allege took place here.[15] Thus, contrary to Plaintiffs' unsupported assertions, USAA's supposed failure to refer to possible arguments for retaining federal jurisdiction cannot serve as a basis for sanctions.

*Second*, in any event, the factual premise of Plaintiffs' recasted sanctions argument – that USAA failed to direct this Court's attention to any of the cases in which it had litigated in federal court (Supp. Br. 8-9) – is incorrect. In its motion to dismiss this case, USAA placed almost exclusive reliance on the Tenth Circuit's *Tuck* decision, noting that "*Tuck* is directly on point [and involved] the identical question against the identical defendant." Mem. of Points and Authorities at 5. USAA thus directly referred the Court to, and endorsed, the Tenth Circuit's discussion of USAA's jurisdictional status. In *Tuck*, the court expressly noted:

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[15] In addition, Plaintiffs discuss (Supp. Br. 3-4) *Eash v. Riggins Trucking Inc.*, 757 F.2d 557, 567 (3d Cir. 1985), but only for the unexceptional proposition that federal courts have the inherent authority to impose sanctions. Similarly, Plaintiffs cite (Supp. Br. 5-6) *In re Itel Sec. Litig.*, 791 F.2d 672 (9th Cir. 1986), *cert. denied*, 479 U.S. 1033 (1987), only for the general standard that must be met before sanctions should be awarded pursuant to the courts' inherent authority.

Nor does the Supreme Court's recent sanctions decision in *Chambers v. Nasco, Inc.*, 111 S.Ct. 2123, 2138 (1991) – a case Plaintiffs do not cite – have any bearing here. In *Chambers*, the attorney was sanctioned for, inter alia, telling the trial court that no temporary restraining order was necessary in a suit for specific performance of a contract to sell real estate because no transfer of the properties was in process, when in fact he had already begun arrangements to have the real estate transferred into a trust to put them beyond the reach of the plaintiff. *See id.* at 2128-29.

> the fact that USAA has appeared in federal courts under their diversity jurisdiction, even after the decision in *Baer*, both as plaintiff and defendant, and the question of USAA's corporate status and citizenship was apparently not considered. . . . A few of these cases even recite erroneous findings regarding USAA's diversity status.

859 F.2d 845 n.3 (citations omitted). Not only did the Tenth Circuit discuss the very issue Plaintiffs claim USAA failed to point out to this Court, but it cited some of the very cases that Plaintiffs have included their addendum in support of the request of sanctions. *See id.* (citing *Moore v. USAA*, 819 F.2d 101 (5th Cir. 1987) (Case No. 44 on Plaintiffs' list); *Boardman v. USAA*, 742 F.2d 847 (5th Cir. 1984) (Case No. 87 on Plaintiffs' list); *USAA v. Cregor*, 617 F. Supp. 1053 (N.D. Ill. 1985) (Case No. 52 on Plaintiffs' list)). Thus, USAA referred this Court to *Tuck*'s discussion of precisely what Plaintiffs now complain should have been disclosed – *i.e.*, "USAA's . . . conduct in other cases." Supp. Br. 8. Since Plaintiffs themselves suggest (Supp. Br. 9) that a motion to dismiss which presents the "conflicting rulings" would be appropriate, then by their own standard, their effort to collect sanctions collapses.

*Finally*, USAA wishes to make clear that it regrets its failure in the past to closely monitor diversity cases in federal court. Following *Tuck*, USAA has moved to correct the deficiencies that allowed the problems to continue. For example, on May 2, 1988 – following its notice to the Tenth Circuit in *Tuck* of the jurisdictional issue and even before the Tenth Circuit's decision – USAA sent a special bulletin on the jurisdictional issue to all regional claims

officials. The bulletin cited *Baer* and instructed these personnel to "take appropriate action to seek dismissal based on the lack of diversity."[16] Then, after the court's strong admonition in the October 14, 1988 *Tuck* decision "to make similar motions [to dismiss] in all pending diversity litigation" (859 F.2d at 845 n.3), USAA reiterated the message on December 12, 1988, in a special memorandum to all senior claims attorneys and supervisors of litigation. The memorandum advised each recipient "to review the *Tuck* decision," and noted that "[t]he court is very strong in its position regarding USAA litigating in Federal Court." Report at 4 (quotations omitted). The memorandum then emphasized that "all future cases will be handled in accordance with the *Baer* decision and the *Tuck* decision." *Id.* (quotations omitted).[17]

When USAA discovered during the second appeal in *Tuck* that its earlier actions had not been sufficient to prevent its participation in federal diversity cases,[18] it promptly took additional steps, which it reported to the Tenth Circuit on December 10, 1990. USAA revised its

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[16] The bulletin is quoted in USAA's report to the Tenth Circuit (the "Report"), a copy of which was filed with USAA's reply memorandum in this case, as Exhibit A to the Declaration of Timothy B. Dyk.

[17] USAA followed up this memorandum with a discussion at a May 10, 1989 legal conference for senior claims attorneys, supervisors of litigation, and regional claims management personnel of the need to ensure that USAA, as an entity, stay out of federal diversity actions. *See* Report at 4.

[18] For example, the appeal in *Transamerica Ins. Group v. Hawaiian Ins. & Guaranty Co.*, 889 F.2d 1096 (9th Cir. 1989) (table), remained pending even after the *Tuck* decision, becoming final on November 21, 1989.

internal docketing procedures and case-tracking system in order to identify cases pending in federal court. Moreover, because the post-*Tuck* cases suggested that local counsel were not being adequately informed of USAA's policy not to litigate in federal court, USAA undertook another round of special notices and bulletins on the jurisdictional issue, this time focusing on the more than 3200 outside counsel that handle litigation for USAA. These outside counsel were sent two special notices on the jurisdictional issue, and were asked to identify any pending federal court cases.[19] In an effort to avoid and detect federal court diversity filings, USAA is annually notifying its outside counsel and claims personnel to stay out of federal court in diversity cases. In addition, USAA is annually reviewing the docketing system in each federal court in the United States to detect any diversity cases that have been filed so that such cases promptly can be dismissed.[20] USAA's actions in this case are part of

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[19] While all outside counsel on USAA's list of approved counsel were so notified, USAA recently has noted that counsel not on the approved list sometimes are retained, and USAA has taken steps to send these counsel the same notices received by counsel on the approved list.

[20] of course, additional cases continue to be filed in federal court against USAA, and despite USAA's memoranda instructing its outside counsel not to file in federal court, counsel occasionally have filed diversity cases on USAA's behalf in federal court. Following the Report to the Tenth Circuit, with one exception, a motion to dismiss or stipulated dismissal was filed in these cases at an early stage, before any decision on the merits. The exception is *Krstich v. USAA*, 1991 U.S. Dist. LEXIS 15746 (N.D. Ohio June 10, 1991), which was filed on October 30, 1989 by an insured basing jurisdiction on diversity of

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this established policy to comply with *Carden* and *Tuck*, and should not serve as the basis for any award of sanctions.

## III. Restructuring This Case As a Class Action Is Legally Impermissible And Would Not Promote Judicial Economy

Perhaps recognizing that their basic argument for retaining jurisdiction is foreclosed by *Carden*, Plaintiffs next suggest (Supp. Br. 24-33) that they be allowed to amend their complaint to correct the "jurisdictional flaws" by restructuring the entire case as a class action against USAA's individual members. Regardless of whether this approach would solve the diversity problem,[21] it is impermissible and unwarranted.

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citizenship. A final judgment in *Krstich*, adverse to USAA, was entered on June 10, 1991. *Krstich* unfortunately was not discovered by USAA's management until recently.

[21] USAA believes that it would not cure the jurisdictional problem. Plaintiffs cite *Supreme Tribe of Ben-Hur v. Cauble*, 255 U.S. 356 (1921), for the proposition that the citizenship of a class is determined solely by reference to the class representative. But *Supreme Tribe of Ben-Hur* was not a case against an unincorporated association styled as a class action only to create diversity in a suit that was in essence against the entity itself. In such situations, USAA believes that the governing standard is the Supreme Court's recent directive in *Carden* that "to determine, for diversity purposes, the citizenship of an artificial entity, the court [must] consult the citizenship of . . . 'all the [entity's] members.' " 194 U.S. at 195. An attempt to avoid *Carden* by dismissing non-diverse members of the class,

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A. The Federal Rules Of Civil Procedure Do Not Authorize The Class Action That Plaintiffs Propose

The Federal Rules of Civil Procedure authorize a class action against the individual members of an unincorporated association only when the association cannot be sued as an entity under the applicable state law. Specifically, while Rule 23.2 provides a limited mechanism for a class action against the members of an unincorporated association, the Advisory Committee Note makes it clear that the Rule has limited applicability:

> Although an action by or against representatives of the membership of an unincorporated association has often been viewed as a class action, the real or main purpose of this characterization has been *to give "entity treatment" to the association when for formal reasons it cannot sue or be sued as a jural person under Rule 17(b)* [citations omitted] . . . . Rule 23.2 deals *separately* with these actions, referring where appropriate to Rule 23.

Fed. R. Civ. P. 23.2, Advisory Committee Note (emphasis added). Thus, the Note makes clear that Rule 23.2 is designed to deal "separately" with situations in which "the association . . . for formal reasons . . . cannot sue or

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as was done by the district court on remand in *Tuck* (*see Tuck v. USAA*, 722 F. Supp. 100, 102 (N.D. Okla. 1989)), would only lead to further problems concerning the apportionment of any judgment among the diverse and non-diverse members of USAA.

be sued as a jural person under Rule 17(b)." *Id.* That is not the situation here.

Rule 17(b) provides that an unincorporated entity's capacity to be sued is determined "by the law of the state in which the district court is held." Here, as Plaintiffs themselves pointed out in their initial memorandum in opposition (Mem. 24), California law authorizes unincorporated reciprocal exchanges such as USAA to sue and be sued in their own name. *See* Cal. Ins. Code § 1450.[22] Indeed, under California law, an action, such as Plaintiffs seek to create, against the individual subscribers to a reciprocal exchange is not permitted unless "a final judgment has been obtained against the exchange and remains unsatisfied for 30 days." *Id.* § 1451. Because USAA therefore can, and must, "be sued as a jural person," a Rule 23.2 class action is not available. *See* Fed. R. Civ. P. 23.2, Advisory Committee Note.

The overwhelming majority of courts to consider the question have adopted precisely this reading of Rule 23.2 and rejected attempts, like that of Plaintiffs here, to restructure suits against artificial entities as class actions when state law gives those entities the capacity to be sued in their own right. For example, the First Circuit, *Northbrook Excess & Surplus Ins. Co. v. Medical Malpractice Joint Underwriting Ass'n of Mass.*, 900 F.2d 476, 478 (1st Cir. 1990), adopted the Advisory Committee Note's limitation and held that "[r]ule [23.2] may not be used merely to create diversity jurisdiction . . . [because] the

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[22] Texas law also gives a reciprocal exchange the right to sue and be sued in their own name. *See* Tex. Rev. Civ. Stat. Ann. art. 6137.

rule's purpose is to give entity treatment to unincorporated associations where state law does not permit them to sue or to be sued." Moreover, the *Northbrook* Court noted that "most courts that have examined the scope of Rule 23.2's availability" have reached the same conclusion: "where an association has jural status under state law, the rule does not come into play." *Id.* at 478 (citing cases); *accord, e.g., Patrician Towers Owners, Inc. v. Fairchild*, 513 F.2d 216, 220 (4th Cir. 1975); *National Bank of Washington v. Mallery*, 669 F. Supp. 22 (D.D.C. 1987); *Lang v. Windsor Mount Joy Mut. Ins. Co.*, 493 F. Supp. 97 (E.D. Pa. 1980); *Gay Liberation v. University of Missouri*, 416 F. Supp. 1350 (W.D. Mo. 1976), *rev'd on other grounds*, 558 F.2d 848 (8th Cir. 1977), *cert. denied*, 434 U.S. 1080 (1978); *Lee v. Navarro Savings Ass'n*, 416 F. Supp. 1186 (N.D. Tex. 1976), *rev'd on other grounds*, 597 F.2d 421 (5th Cir. 1979), *aff'd*, 446 U.S. 458 (1980); *Suchem, Inc. v. Central Aguirre Sugar Co.*, 52 F.R.D. 348 (D.P.R. 1971). Thus, both Rule 23.2 and the case law make clear that Plaintiffs' attempt to restructure this suit as a class action should be rejected.

Plaintiffs offer only two arguments in support of their construction of Rule 23.2. Neither withstands analysis.

*First*, Plaintiffs (Supp. Br. 28-30) distort the meaning of the Advisory Committee Note, which even they concede (Supp. Br. 28) must be consulted in construing Rule 23.2. Specifically, Plaintiffs suggest (Supp. Br. 29) that, although the Note says the mechanism established in rule 23.2 is intended "to give 'entity treatment' to [an] association when for formal reasons it cannot sue or be sued as a jural person," the Note really means that "the class action

device should be generally available." Plaintiffs' sole support for this effort to turn the Advisory Committee Note on its head is the Note's citation of *Oskoian v. Canuel*, 269 F.2d 311 (1st Cir. 1959). But *Oskoian* was cited by the Advisory Committee in *support* of the proposition set forth in the Note – namely, that the class action mechanism is available only when the entity lacks jural status under state law – and in fact does support that proposition.[23] Under the Rhode Island law at issue in *Oskoian*, a suit against the unincorporated entity per se was not authorized. That statute, rather, permitted only an action against all the members of the association, or against the officers " 'as the representative or representatives of such association.' " 269 F.2d at 314 (quoting R.I. Gen. Laws § 9-2-12). Thus, Rhode Island presented precisely the situation in which the Advisory Committee called for use of the class action device: state law did not give the association the right to sue or be sued as a jural person. *See* Fed. R. Civ. P. 23.2, Advisory Committee Note.[24] Plaintiffs' attempt to rely on *Oskoian* as a basis to ignore the Advisory Committee Note therefore is without support.

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[23] The other two cases cited by the Advisory Committee also support the proposition that a class action is available when state law prevents a suit against the entity itself. *Gibbs v. Buck*, 307 U.S. 66, 69 (1939) (Florida law made the association unlawful); *Tunstall v. Brotherhood of Locomotive F. & E.*, 148 F.2d 403, 405 (4th Cir. 1945) (West Virginia law barred suits by the entity in its own name).

[24] This is the same reading of *Oskoian* that the First Circuit itself adopted in *Northbrook*. Plaintiffs' suggestion (Supp. Br. 30) that *Northbrook* improperly distinguished *Oskoian* thus is unavailing.

*Second*, Plaintiffs point repeatedly (Supp. Br. 25, 27, 29, 32) to *Curley v. Brignoli, Curley & Roberts Assocs.*, 915 F.2d 81 (2d Cir. 1990), *cert. denied*, 111 S.Ct. 1430 (1991), and *Kerney v. Fort Griffin Fandangle Ass'n, Inc.*, 624 F.2d 717 (5th Cir. 1980), and argue that these cases strongly support use of the class action device here. In fact, however, these decisions are readily distinguishable. In both cases, restructuring the suit as a class action was necessary to enable the plaintiffs to secure full relief. For example, *Curley* was a suit by the limited partners of a limited partnership for breach of fiduciary duty by the general partner. *Id.* at 82-83. The limited partners originally filed their suit derivatively, with the partnership itself named as a party. *Id.* But application of *Carden*'s citizenship rule to the partnership destroyed diversity, and when the jurisdictional issue was raised for the first time on appeal, the court ruled that the case should be restructured as a class action. *Id.* at 83-84. While disagreeing with *Northbrook*'s reading of Rule 23.2, the court in *Curley* also based its decision on New York partnership law, which required that plaintiffs use the class action mechanism, rather than a derivative suit, to redress breaches of fiduciary duty by a general partner. *Id.* at 87-88. This precise reading of *Curley* recently was adopted by *900 3rd Ave. Assocs. v. Finkielstain*, 758 F.Supp. 928 (S.D.N.Y. 1991). Although it was, of course, bound by *Curley*, the *Finkielstain* Court read *Curley* to authorize a class action only when state law indicated that a class action was the appropriate mechanism for the lawsuit. *See* 758 F. Supp. at 931-32.

Likewise, the court in *Kerney* determined that a class action was necessary to provide full relief under state

law. The court noted that under the relevant state law, "judgment rendered on an entity suit may be enforced against only the association's property and not that of the individual members." 624 F.2d at 720. Thus, *Kerney* approved an amendment converting the suit to a class action to enable the plaintiff to reach assets that otherwise could not be reached. *Id.* Indeed, *Kerney* expressly distinguished a case, such as the one Plaintiffs seek to create here, that is brought as "a class action rather than an entity suit only in order to select diverse parties as named class representatives and thereby create jurisdiction and not in order to obtain different relief." *Id.* at 720 n.6. Thus, neither *Curley* nor *Kerney* supports the procedural maneuvering that Plaintiffs seek to employ.

B. Plaintiffs' Class Action Approach Would Nullify The Supreme Court's Decision In Carden

Plaintiffs' last-minute attempt to alter the entire structure of this lawsuit by targeting USAA's individual members, rather than the entity itself, is an attempt to evade *Carden*'s holding. The Supreme Court in *Carden* carefully limited the scope of diversity jurisdiction, and noted that any "further adjustments" of the federal courts' role should "be made by Congress." 494 U.S. at 196. Plaintiffs seek to nullify this judgment through an elaborate procedural maneuver; if, as Plaintiffs suggest, an artificial entity could sue or be sued in diversity merely by characterizing the lawsuit as a class action, the *Carden* decision would be rendered meaningless. Indeed, since it relies on *Curley* – a case involving a limited partnership – plaintiffs' approach is not even limited to

unincorporated associations, but extends instead to all artificial entities other than corporations. Such a use of Rule 23.2 is a direct challenge to *Carden*. The court in *900 3rd Ave. Assocs. v. Finkielstain* recently refused to engage in the exact type of procedural subterfuge suggested by Plaintiffs for precisely this reason; the court decided that allowing creation of federal jurisdiction on this back-door fashion would "subvert the Supreme Court's holding in *Carden*." 758 F. Supp. at 931-32. Plaintiffs' attempt to use Rule 23.2 as a procedural device to get around the binding holding of *Carden* should be rejected. The class action mechanism is not available to a plaintiff "seeking to employ Rule 23.2 merely to manufacture diversity jurisdiction." *Northbrook*, 900 F.2d at 479.

C. Use Of A Class Action Mechanism Is Not Warranted In This Case

In all events, use of the class action device suggested by Plaintiffs is not warranted in the circumstances of this case. Plaintiffs argue (Supp. Br. 26) that *Tuck* supports the use of a class action "as a jurisdictional cure for the difficulties caused by [USAA]." But what Plaintiffs neglect to mention is that the only reason the Tenth Circuit in *Tuck* even considered taking this step is that the case had already proceeded through an entire trial, and a jury verdict had been reached, before the jurisdictional issue was uncovered on appeal. *See Tuck*, 859 F.2d at 844.[25] Moreover, in remanding the case, the Tenth Circuit

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[25] Similarly, in *Curley*, the court expressly relied on the importance of preserving "a fully litigated judgment," as a

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noted that "the district court may not be able to find a way" to retain jurisdiction, and that "dismissal of the action" may be required. *Id.* at 846.[26]

Here, no such concerns are implicated. This lawsuit is at its very beginning, and USAA has promptly and properly brought the jurisdictional defect to the Court's attention – as the Tenth Circuit in *Tuck* had expressly instructed it to do. *See Tuck*, 859 F.2d at 845 n.3 (USAA should file "motions [to dismiss] in all pending diversity litigation"). Shifting this litigation to state court would involve no waste of judicial resources, no abandonment of a jury verdict, no extra expense, and no unfairness to any of the parties.

Indeed, in the circumstances of this case, it is proceeding if federal court that would impose a substantial burden. Plaintiffs seek to create an unwieldy class action involving hundreds of thousands of individual members of USAA. *See* Affidavit of Thomas J. Corridan (submitted with Motion to Dismiss) (noting that USAA has 186,556 members domiciled in California alone). Maintenance of such an action would impose on the Court and the parties

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basis for recharacterizing the suit as a class action. *See* 915 F.2d at 91 (quotations omitted).

[26] The district court, in restructuring the case as a class action, did not have the benefit of the First Circuit's 1990 decision in *Northbrook*. Indeed, USAA had appealed the district court's decision to create a class action and intended to argue that the class action device was not available under Rule 23.2 and the recently-decided *Northbrook* case. *Tuck* was settled, however, before the briefing was completed and the Tenth Circuit never addressed the class action issue.

enormous procedural and administrative burdens concerning issues such as notice to class members. Specifically, by its terms, Rule 23.2 would require compliance with the notice provisions set forth in Rule 23(d) and (e). Rule 23(d) authorizes the court to:

> requir[e], for the protection of the members of the class of otherwise for the fair conduct of the action, that notice be given . . . to some or all of the members of any step in action, or of the proposed extent of any judgment, or of the opportunity of members to signify whether they consider the representation fair and adequate, to intervene and present claims or defenses, or otherwise to come into the action.

Fed. R. Civ. P. 23(d)(2). If this case were transformed into a class action, this Court therefore would be required to determine whether notice of any one of a host of steps in the litigation should be given to class members in order to meet due process standards, and then to determine what form that notice should take. *See* 7B C. Wright, A. Miller & M. Kane, *Federal Practice and Procedure* § 1793, at 299-300 & nn. 17-18 (2d ed. 1986).[27]

Rule 23(e) imposes even more substantial burdens. Under this provision, notice of dismissal or settlement of a class action is mandatory:

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[27] There is a split of authority concerning whether at least some form of notice is required as a constitutional minimum in all cases. *See* 7B C. Wright, A. Miller & M. Kane, *Federal Practice and Procedure* § 1793, at 299-300 & nn. 17-18 (2d ed. 1986) (citing cases).

> A class action shall not be dismissed or compromised without the approval of the court, and notice of the proposed dismissal or compromise *shall be given to all members of the class* in such manner as the court directs.

Fed. R. Civ. P. 23(e) (emphasis added). As the Ninth Circuit has noted, "[a]lthough the rule accords a wide discretion to the District Court as to the form and content of the notice, due process *requires its presence and constitutional adequacy.*" *Mendoza v. United States*, 623 F.2d 1338, 1350-51 (9th Cir. 1980) (emphasis added), *cert. denied*, 450 U.S. 912 (1981); *accord, Officers for Justice v. Civil Serv. Comm'n*, 688 F.2d 615, 624-25 (9th Cir. 1982), *cert. denied*, 459 U.S. 1217 (1983). Thus, if this case were converted into a class action, each of USAA's hundreds of thousands of members might have to receive some form of notice before the suit could be settled. The cost and inevitable delay involved in formulating and disseminating such notice may significantly impact the prospects of any voluntary resolution of this suit, and certainly would force the parties and the Court to devote time and energy to the resolution of ancillary issues.

Given the ready availability of an alternate, state court forum and the very early stage of this litigation, there is no need for this Court to engage in what the *Finkielstain* Court, in rejecting a similar request, labeled an "awkward procedural exercise." 758 F. Supp. at 932. Instead, this Court should grant USAA's motion to dismiss and let this litigation proceed in state court.

## CONCLUSION

For the foregoing reasons, USAA's motion to dismiss for lack of subject matter jurisdiction should be granted, and Plaintiffs' request for sanctions should be denied.

Respectfully submitted,

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## PROOF OF SERVICE

STATE OF CALIFORNIA )
) ss.
COUNTY OF LOS ANGELES )

I am employed in the County of Los Angeles, State of California. I am over the age of eighteen and not a party to the within action; my business address is 3580 Wilshire Boulevard, Los Angeles, California.

On December 30, 1991, I served the foregoing document described as **DEFENDANT'S SUPPLEMENTAL BRIEF IN SUPPORT OF MOTION TO DISMISS FOR**

**LACK OF SUBJECT MATTER JURISDICTION AND IN OPPOSITION TO REQUEST FOR SANCTIONS** on the interested parties in this action by placing a true copy thereof enclosed in a sealed envelope(s) addressed as follows:

William M. Shernoff
Shernoff, Bidart & Darras
600 South Indian Hill Blvd.
Claremont, CA 91711-5498

I delivered such envelope(s) by hand to the offices of the addressee(s).

I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made. Executed on December 30, 1991, at Los Angeles, California.

Type or Print Name

/s/ Thomas Smith
Signature

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. 91 3615 WFN<br><br>PLAINTIFFS' SUPPLEMENTAL REPLY MEMORANDUM OF POINTS AND AUTHORITIES RE: OPPOSITION TO MOTION TO DISMISS<br><br>(Judge Wm. Fremming Nielsen) |

1.

INTRODUCTION

UNITED SERVICES AUTOMOBILE ASSOCIATION (hereinafter "USAA") states that LAUGHLIN E. WATERS and VOULA D. WATERS (hereinafter the "WATERS")

appear to agree with it that this court lacks subject matter jurisdiction unless USAA is a corporation under Texas law and that sanctions cannot be awarded unless USAA acted improperly in this action. USAA is dead (sic)

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1.

## INTRODUCTION

UNITED SERVICES AUTOMOBILE ASSOCIATION (hereinafter "USAA") states that LAUGHLIN E. WATERS

and VOULA D. WATERS (hereinafter the "WATERS") appear to agree with it that this court lacks subject matter jurisdiction unless USAA is a corporation under Texas law and that sanctions cannot be awarded unless USAA acted improperly in this action. USAA is dead wrong. USAA mischaracterizes the WATERS' position apparently in the hope of distracting this court from the WATERS' true positions and serious charges.

USAA's supplemental brief attempts to put the best face it can on its years of misconduct in manipulating the federal courts and litigants. The closest it comes to any remorse for causing untold hours, weeks, and months of wasted judicial resources is its half-hearted statement that it "acknowledges that its past record in this regard has been flawed." Incredibly, USAA is still tap-dancing in an effort to avoid being sanctioned for a pattern of serious misconduct.

So that USAA cannot misconstrue the WATERS' position concerning sanctions and jurisdiction, we will put forth our position in as crystal clear language as possible. We do not want the true perspective and importance of this issue lost in the technical arguments USAA throws at this court.

2.

## THE SANCTIONS ISSUE IN PERSPECTIVE

USAA implies that it brought to the attention of this court its history of contradictory, and indeed fraudulent, jurisdictional statements over a period of years which resulted in massive waste and inconsistent decisions. It

claims it did this by simply citing *Tuck v. USAA*, 859 F.2d 842 (10th Cir. 1988), in its initial dismissal papers because "the issue of USAA's jurisdictional status and history of litigation in federal court" was discussed in *Tuck*. Nothing could be more misleading. USAA was not a volunteer in bringing its pattern of misconduct to any court's attention. In fact, USAA's years of misconduct would still be undetected by the *Tuck* court and *this* court had it not been for a massive investigation carried on by the attorneys handling the *Tuck* case and *this* case which revealed USAA's fraudulent activity. Amazingly, 172 cases of misconduct were unearthed. All of that work was painstakingly retrieved from 52 clerks of 52 federal district courts which were affected by the scheme. Voluminous records were searched and copied from district courts around the country. This investigation took over 100 hours of attorney and paralegal time to simply ferret out and gather the evidence of contradictory jurisdictional affidavits. That is how this scheme was brought to the attention of the federal judiciary. In no way, shape or form did USAA attempt to come forward or police itself until it was *caught* as a result of this investigation.

Even after being caught, USAA was not repentant. It fought the suggestion of sanctions by the Tenth Circuit Court of Appeals tooth and nail. Upon remand in *Tuck*, USAA fought vigorously the idea that the federal district court in *Tuck* could sanction it for its misconduct. It also fought vigorously the notion that the complaint in *Tuck* could be amended to preserve jurisdiction (just as it is doing in this case). When all of its efforts in *Tuck* failed, it then did the last thing it could possibly do to avoid having its misconduct sanctioned. After almost five years

of hard-fought litigation it threw over $1 million at the plaintiff's lawyers in the *Tuck* case to settle that case. In that way, it avoided the sanctions motion being ruled by the court in *Tuck*.

USAA erroneously asserts that the WATERS' position is that "sanctions cannot be awarded against USAA unless USAA acted improperly in this action." That is a mischaracterization of the WATERS' position. Attorneys and litigants have been sanctioned by the federal courts for as little as filing a misleading paper or wasting one day of court time. Compare that to what we have here. We have uncontroverted evidence of a *pattern* of conduct spanning *years* and involving multiple courts, litigants and parties. This is not an isolated matter. This is a major scheme that has just recently come to the surface.

Plaintiffs' position is simply this: When you have a pattern of misconduct that calls out for sanctions, it matters not whether the misconduct is discovered on the third day of the pattern, the third month of the pattern, or at the end of the third year of the pattern. Once the pattern of misconduct is brought to the attention of the federal judiciary, the judiciary must have the power to police such misconduct or the system will lack integrity and be susceptible to manipulation. In this case, USAA's pattern of misconduct has even continued a considerable time past the *Tuck* court directive. Plaintiffs have pointed out the Hawaii action wherein USAA took a $300,000 judgment, contrary to the instructions of the Tenth Circuit in *Tuck* and USAA has now revealed, at this late date, it has continued into 1991 with a federal district court case in North Dakota.

The sole excuse USAA offers is that it is a large insurer with over 3,000 outside counsel to manage its over 15,000 cases and that the handling of this bureaucratic task has caused these problems. It implies this all happened by inadvertence. This does not sound like a party who is truly sorry for causing so many problems with courts and litigants, all to USAA's advantage. Moreover, this claim of bureaucratic bungling is simply not credible and is yet another form of attempting to whitewash and minimize a most serious matter.

Let's face it, USAA knew it was a reciprocal inter-insurance exchange since it was formed. It knew the unique nature of this hybrid type of entity. It was the expert in reciprocal inter-insurance exchanges. Certainly, neither the federal courts, state courts, nor unsuspecting policyholder litigants knew, or even had a hint of, the fact that USAA could put two faces on its entity status in order to take advantage of the courts and its adversaries. It was USAA's responsibility *from the beginning* to take a correct and consistent position and to avoid taking unfair advantage of the courts and litigants. It did precisely the opposite. It took advantage at every turn and every opportunity, to the financial detriment of its adversaries and to its own financial advantage. It perpetuated this scheme for years (without any memos to outside counsel) until a couple of enterprising lawyers embarked upon a wide-scale investigation and uncovered USAA's sordid activities.

*Even more telling*, USAA's claims of bureaucratic snafu ring hollow in light of the opinion of Judge Mazzone issued in February, *1984*, in *Neil v. USAA*, United States District Court, District of Massachusetts,

Civil Action 83-2414-MA. (A true and correct copy is attached as Exhibit C.) In that declaratory relief action USAA filed a motion to dismiss after an adverse ruling. In that case, Judge Mazzone granted the motion, but noted:

> In [granting the dismissal], however, I must comment that it would behoove the Defendant to act properly and consistently in challenging diversity jurisdiction over it in Federal Court actions. In the past, the Defendant has both sued and allowed itself to be sued in Federal Court where jurisdiction was founded on diversity of citizenship, without challenging jurisdiction as it does in this present motion. [Citations omitted.] Selective challenges to jurisdiction bespeak a self-serving abuse of the Federal Court processes. Such tactics are particularly odious, since subject matter jurisdiction is not a matter that can be created by laches, waiver or estoppel. [Citations omitted.] Had the Defendant acted properly in challenging jurisdiction, substantial expense and effort to the Plaintiff, as well as to the Third-Party Defendants, would have been avoided."

USAA did not mention it, but the truth is, and USAA knows it, USAA was sternly warned by Judge Mazzone about its jurisdictional ploys and admonished to clean up its act *more than 7 years ago*. Yet it was not until *four years later*, in response to the *Tuck* court's admonishment, that USAA sent its first claim department bulletin in May, 1988. It is inconceivable that USAA and its litigation staff was so uninformed about what was going on in the cases involving it that it was unaware of or overlooked Judge Mazzone's warning. Despite USAA's contention of

bureaucratic mistake, the evidence is clear that USAA's jurisdictional manipulations were not mere error but were part of a comprehensive and systematic program that benefited USAA and cost its adversaries and the taxpayers dearly.

USAA now argues that there is some kind of statute of limitations for sanctioning its misconduct. This is an interesting theory, but it has no basis in logic or justice.

The common thread that runs through all of USAA's misconduct is its intentional nondisclosure of the unique status of a reciprocal exchange and the complete nondisclosure of its contradictory positions over the years. It goes without saying that this court would not be aware of the unique nature of a reciprocal inter-insurance exchange under Texas law or of USAA's past jurisdictional hopscotching if the WATERS had not brought this to the court's attention.

Although the nexus between USAA's pattern of misconduct over the years and this case is not overwhelming, the connection clearly exists. This case comes at the tail end of years of blatant misconduct where every instance of jurisdictional misstatements would in and of itself warrant sanctions but for the fact that those misdeeds were undetected at the time. Only USAA knew of its grand design of putting two faces on its entity status in order to take advantage of its adversaries and the courts. It never came forward in an honorable manner. USAA utterly failed to inform this court of the totality of a truly amazing situation.

This sanction motion comes at a time when the scheme is at an end due to being uncovered. USAA has

not yet been sanctioned one penny for its misdeeds. The government must be reimbursed for the tremendous waste of precious judicial time and resources. The WATERS, and their counsel, should be compensated for the investigation of the scheme and for bringing the wrongdoer to account. It goes without saying that the process by which we all litigate must be fair and free of abuse. Almost all federal judges are committed to this cardinal principle, especially in this time of heightened judicial activity. It is vitally important that abuses of the federal process be sanctioned. It is even more critical that major abuses that affect not only the courts, but the public at large, be dealt with severely.

If USAA's position is adopted, the federal courts are powerless to sanction such a continued pattern of serious misconduct as revealed in this case. Such a result would be untenable. Likewise, a result which would allow USAA to escape from compensating the U.S. government for massive judicial time wasted due to its own admitted "flawed record" would be untenable. If it was USAA's vast bureaucracy due to its largeness that caused all of these problems[1], then it should pay the price caused by its own design or failure to implement workable systems which resulted in its wanton disregard for the judicial processes. This is particularly true when the problems that have been caused have all shaken down to the financial advantage of USAA and to the financial disadvantage of its adversaries. One of the biggest victims of this scheme has been the over-burdened federal court who

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[1] As we have discussed above, the evidence is overwhelming that the scheme was done knowingly and by design.

unknowingly fell prey to countless days and weeks of totally wasted judicial resources. Instead of apologizing, after being caught, USAA arrogantly tells this Court, as it did the *Tuck* court, that the Court has no jurisdiction or power to sanction it for its misconduct. The WATERS are confident that this court will find the correct way to deal with this situation so that all concerned, litigants and the public, will have confidence in the integrity of the federal court system.

3.

USAA'S OPPOSITION TO SANCTIONS FAILS TO DEMONSTRATE EITHER THAT THE COURT IS WITHOUT INHERENT POWER TO SANCTION IN THIS CASE OR THAT SANCTIONS ARE UNDESERVED

USAA's opposition chooses to attack only factual bases for the sanction cases cited by plaintiffs without addressing the portent of those cases and the applicability of the philosophy expressed in those cases to the facts in this case. USAA attempts to focus this Court's attention on the trees in the hopes that the forest will be bypassed.

Obviously, the cases cited in plaintiffs' brief are *factually* dissimilar to the present case. As noted by plaintiffs at every turn, the facts in this case are, hopefully, unique. There is no other known case in which the manipulation of the entire federal court *system* has been so pervasive, blatant and extensive.

Thus, the various factual backgrounds in the cases cited by plaintiffs are far less important than the philosophy expressed in those cases and application of

the general rule of law as demonstrated by those cases. USAA cites not a single case which holds that this court does *not* have an inherent power to sanction in this situation. Moreover, the cases cited by plaintiff, while factually dissimilar, stand for the proposition that a party can be sanctioned in one case for conduct outside *that* case and for conduct before a *different* court. (See *In Re Itel Securities Litigation*, 791 F.2d 672 (9th Cir. 1986); *Freeze v. Griffith*, 849 F.2d 172 (5th Cir. 1988) and *Moody v. Miller*, 864 F.2d 1178 (5th Cir. 1989).)[2]

It is also important to note that USAA did not address or object to plaintiffs' citation of authority that this court may sanction USAA in this case even if the action is dismissed and relegated to state court. That can only be a concession by USAA that plaintiffs' position is correct.

The critical and essential consideration in regard to the sanctions issue is the acknowledgment that if this court cannot or does not sanction USAA, then no court can. USAA will have escaped unscathed.

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[2] Similarly, a California state court judge recently imposed sanctions on an insurer in one case for filing an action in another court. As discussed in the article, attached as *Exhibit A*, a Los Angeles Superior Court judge awarded the Department of Insurance sanctions of between $5000 and $10,000 against an insurer for the insurer's conduct in filing an action against the Department in San Francisco despite the Supreme Court's order that all such suits should be filed in Los Angeles.

4.

UNDER *CARDEN*, USAA MUST BE CONSIDERED A CORPORATION FOR DIVERSITY JURISDICTION PURPOSES

USAA cites the *Carden v. Arkoma Associates*, 494 U.S. 185, 110 S.Ct. 1015 (1990) decision quite frequently, as if *Carden* stands for an endorsement of its years of misconduct. Noteworthy is the fact that the *Carden* case was not even mentioned by USAA in its original motion to dismiss. *Carden* does not stand for the proposition that USAA can manipulate and defraud courts and litigants to its own advantage and get away with it. Neither does *Carden* stand for the sweeping proposition for which USAA cites it.

It must first be acknowledged that the 5-4 decision in *Carden* is a narrow one. As noted by Justice Scalia in his opening paragraph:

> "The question presented in this case is whether, in a suit brought by a limited partnership, the citizenship of the limited partners must be taken into account to determine diversity of citizenship among the parties." (*Carden, supra*, 110 S.Ct. at 1016.)

*Carden* stands only for the narrow proposition that while a corporation can be considered a "citizen" of a state for purposes of diversity jurisdiction, other entities will be treated differently. But *Carden* does not address, and gives no guidance for the determination of, the question presented here: What *is* a "corporation" for diversity jurisdiction purposes?

There are many types of corporations. There are open and closed corporations, there are profit and nonprofit corporations, there are stock and mutual corporations as well as a host of other varieties of corporations. All have the singular benefit of no personal liability for the members that constitute the corporate body. Texas classifies a reciprocal inter-insurance exchange as a corporation and limits its members' liability (Texas Insurance Code, Article 19.03(3)) just as it does other corporations.

The only way to determine what is, or is not, a corporation is to look to state law. In this case, Texas law is clear. USAA is deemed a corporation by statute.

USAA talks out of both sides of its mouth. First it says that, under the diversity rules, only something which is *called* a corporation can be a corporation. Then, it argues that simply because USAA is *called* a corporation under the Texas statutes does not mean it *is* a corporation. Either *Carden* must be read to permit federal jurisdiction whenever an entity is *called* a corporation or *Carden* must be read to authorize an examination of whether the entity is, in substance and in fact, a corporate entity. Under either application of *Carden*, USAA loses.

Although USAA contends that the statute under which USAA is defined as a corporation is very narrow, that simply does not overcome the fact that USAA is expressly defined as a corporation. Additionally, the relevant statute deals with a critically important and integral issue in regard to corporate issue: individual liability of directors. The fact that an inter-insurance exchange is

granted the same immunity as are other types of corporations is a significant indication of its status as a type of corporation.

USAA's additional argument that because USAA is not, in every respect, treated like other corporations in regard to other regulatory provisions is of no avail. The fact is, there are numerous *types* of corporations in every state's law. For example, there are various types of both for-profit and non-profit corporations, each subject to differing regulations and requirements. Similarly, there are varying types of insurance corporations, some subject to certain regulatory provisions (e.g., health maintenance organizations) which others are not. The fact that there are species of corporations which are subject to different regulations does not overcome the ultimate fact that USAA is expressly defined under Texas statutes as a corporation. If it is a corporation for Texas, it is a corporation for this Court and USAA's semantic games cannot change that fact.

5.

## THERE HAS BEEN NO JUSTIFIABLE BASIS PRESENTED BY USAA TO PRECLUDE USE OF THE CLASS ACTION DEVICE TO MAINTAIN JURISDICTION IN THIS CASE

First, a factual misrepresentation made by USAA must be disclosed. In attempting to distinguish *Oskoian v. Canuel*, 269 F.2d 311 (1st Cir. 1959), USAA contends that the class action was permitted only because Rhode Island law did not grant the entity jural status. That is false. In fact, Rhode Island *did* grant jural status to the entity involved. However, the plaintiff had failed to follow the

procedure necessary to prosecute the entity under that statute.

USAA acknowledges that in *Kerney v. Fort Griffin Fandangle Association, Inc.*, 624 F.2d 717 (5th Cir. 1980) the court authorized the use of the class action device because the relevant state law provided that "judgment rendered on an entity suit may be enforced against only the association's property and not that of the individual members." Yet USAA ignores that its members enjoy the same immunity. As provided in USAA's own Subscriber's Agreement (see Exhibit B), each member's liability is limited. Thus, as in *Kerney*, class action is the proper device to avoid the limitation of liability otherwise permitted.

Even if the special class action rule for unincorporated associations were not applicable to this case because USAA can be sued as an entity under California law, that does not preclude the maintenance of a class action under the general class action rule, Rule 23. Nothing in that rule restricts its application in this case. Moreover, an action under Rule 23(b) (1) has expressly been used in cases in which the defendant is an unincorporated association. (*Management Television Systems, Inc. v. National Football League*, 52 F.R.D. 162 (E.D. Pa 1971).) Permitting a class action in this case is only just and fair.

USAA's objections to the use of the class action device in this case are equally unavailing. USAA claims that use of the class action device in this case "would impose on the Court and the parties enormous procedural and administrative burdens." (USAA's Memorandum, page 31, lines 11-12.) Primarily, USAA contends

that the issue of notice would be unreasonably burdensome. However, USAA's own Subscriber's Agreement provides that notice to the attorney-in-fact is sufficient. Thus, notice to the attorney-in-fact should be adequate. Additionally, the fact that the subscriber's individual liability is limited justifies notice limited to the appointed attorney-in-fact. Finally, in a class action brought under Rule 23(b) (1), notice is not even mandatory. (*Hammond v. Powell*, 462 F.2d 1053, 1055 (4th Cir. 1972).) As such, USAA's objections to the class action device are without justification or merit.

6.

ANOTHER ALTERNATIVE FOR RETAINING JURISDICTION IS TO ALLOW PLAINTIFFS TO AMEND THE COMPLAINT TO SUBSTITUTE USAA'S ATTORNEY-IN-FACT AS THE SOLE DEFENDANT

As noted, USAA's Subscriber's Agreement (attached as Exhibit B) expressly provides that USAA's attorney-in-fact may represent the individual subscribers in court and may both sue and *defend on behalf of each subscriber*. This device could thus permit USAA to pursue litigation by naming its attorney-in-fact, a citizen of Texas, and invoking federal diversity jurisdiction in actions against parties who are not Texas citizens. (*Klamath-Lake Pharm. Ass'n v. Klamath Med. Services Bureau*, 701 F.2d 1276 (9th Cir. 1983) [assignee of a claim is real party in interest and may sue in his own name without joining the assignor].) Thus, USAA may continue to use this device to access the federal court system.

That same procedural device could be used to permit plaintiffs to sue USAA by suing its attorney-in-fact, a Texas citizen, as the sole defendant and representative of the subscribers. This would eliminate any possible objection to the class action device, would permit this court to maintain jurisdiction and would permit the parties to proceed to the substantive issues in this action.

## 7.

## CONCLUSION

This case presents an exceptional sanctions issue. There are few, if any, reported appellate decisions involving a pattern of misconduct respecting jurisdictional issues which resulted in financial gain to the perpetrator and in a waste of judicial resources of major proportions. The consequence to the litigants involved undoubtedly involved millions of dollars.

Faced, for the first time, of possibly paying the price of such deception, USAA has not denied the evidence of its misconduct, nor has USAA denied the enormity of the results of its misdeeds. It simply asked this Court to excuse it because it is large and has so many lawyers and cases. Actually, this is a reason to impose sanctions rather than excuse them. USAA has been one of the prime beneficiaries of the federal court system. Any party who uses the court so frequently should bear the responsibility of using it correctly.

USAA's other response is even more alarming. It boldly and unabashedly tells this Court that USAA can waste judicial resources by way of a deceptive scheme

and this Court cannot do anything to rectify the situation, simply because the motion for sanctions is coming at a time when the pattern of misconduct is ending, and in a case where the misconduct is less serious than in previous cases involved in the scheme. That position simply defies logic and justice. Reduced to the bottom line, USAA argues that if you are a very large company and if the deception is so clever that it escapes detection, you are home free. As the WATERS have pointed out, we believe this Court has the inherent power to sanction USAA whether or not it retains jurisdiction.

We believe this Court should retain jurisdiction in this case because a reciprocal inter-insurance exchange is, under Texas law, classified as a corporation and, under *Carden*, is therefore a citizen of the state of Texas for jurisdictional purposes. Accordingly, this Court should look at USAA as a jural person and invoke diversity jurisdiction. This is particularly true because of the 1987 Amendments in the Texas law which deem a reciprocal inter-insurance exchange a corporation. *Baer* and *Tuck* notwithstanding, this is the first court that has been given an opportunity to fully explore the unique nature of a reciprocal inter-insurance exchange, under recent Texas law.

As one alternate way of retaining jurisdiction, this Court can allow plaintiffs to amend their complaint to assert a class action under either Rule 23.2 or 23(b) (1).

As a final, and perhaps most practicable alternative, plaintiffs can be permitted to amend their complaint to name Robert McDermott, the attorney-in-fact for every

USAA subscriber and a Texas citizen, as the sole defendant in this action.

Lastly, even if this Court does not retain jurisdiction, it has the power to sanction USAA for its years of misconduct and should definitely exercise that power in this case in order to validate the integrity of the judicial process.

Dated this 8th day of January, 1992 at Claremont, California.

Respectfully submitted,

SHERNOFF, BIDART & DARRAS

By: /s/ William M. Shernoff
WILLIAM M. SHERNOFF

*Attorneys for Plaintiffs*

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**EXHIBIT A**

THE JOURNAL OF COMMERCE **Thursday, December 5, 1991**

**Court Penalizes Insurer Over Venue Violation**

**By JERRY GOLDBERG**
Journal of Commerce Special

LOS ANGELES – Los Angeles County Superior Court Judge Dzintra Janavs said Tuesday she will impose sanctions against Woodland Hills-based 20th Century Insurance Co. and Gary Fontana, its legal counsel.

Judge Janavs charged the insurer with "attempting to manipulate the judicial process" by filing a Proposition 103-related lawsuit in a San Francisco County Superior Court.

Among other things, the judge said she would issue an order requiring the company to compensate the Department of Insurance for $5,000 to $10,000.

Proposition 103 is the 1988 voter-approved measure calling for the election of state's insurance commissioner, prior approval of rate increases and a rollback of insurance rates.

Judge Janavs imposed the sanctions on the motion of California Insurance Commissioner John Garamendi. The two 20th Century companies were among 14 companies, representing more than half the California insurance market, who were ordered to refund $1.56 billion to 1989 customers by Mr. Garamendi on Nov. 13.

Judge Janavs said the San Francisco suit was in violation of an order by California Supreme Court Chief Justice Malcolm Lucas, which required all California Proposition 103 matters to be filed in Judge Janavs' court.

Judge Janavs ruled 20th Century's lawsuit should have been filed in Los Angeles, and ordered the case transferred to her court.

Justice Lucas' ruling occurred following a period when numerous Proposition 103 lawsuits were filed in San Francisco, Sacramento, San Jose, Los Angeles and San Diego.

Attorneys for Roxani Gillespie, the former insurance commissioner, complained at the time that defending

suits all over the state put excessive costs on the Department of Insurance.

Several California judges also complained that lawyers were attempting to "shop" for judges who would provide favorable rulings.

The suit was filed by 20th Century Insurance Co. and 21st Century Industries, subsidiaries of 20th Century Industries.

20th Century's San Francisco suit against the Insurance Department challenged the method used by Mr. Garamendi in deciding the insurer should return $106.5 million in premiums to customers.

The lawsuit contends the formula used by Mr. Garamendi did not reflect the true cost of insurance premiums to consumers.

It also charged the emergency regulations "essentially sidesteps the process that Prop. 103 called for in rate setting."

Mr. Garamendi said 20th Century had obtained an order from the San Francisco Court setting a hearing on its petition for Dec. 13, which was three days before the administrative hearing was scheduled.

Observers have been puzzled by Mr. Garamendi's rollback order since he issued statistics two weeks before that indicated 20th Century had the lowest premium rate of any personal line insurer doing business in any area of California.

The insurer has a 2.7% share of the California market.

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## EXHIBIT B

### SUBSCRIBER'S AGREEMENT AND POWER OF ATTORNEY

The undersigned, hereafter known as the Subscriber, agrees with other subscribers at an Exchange known as the UNITED SERVICES AUTOMOBILE ASSOCIATION, hereinafter referred to as the Association, located at San Antonio, Texas, to exchange private contracts of indemnity. To that end, I hereby appoint the President of the Association and/or such person or persons as may be designated by the Board of Directors in accordance with Article VIII, Section 8 of the Bylaws, and licensed by the Commissioner of Insurance of the State of Texas, with full powers of substitution and revocation, and with authority to act jointly or severally, as my Attorney-in-Fact, in my name, place and stead, to represent me in the following matters:

1. To exchange with other subscribers at such Exchange, insurance coverages as now or hereafter authorized by the Board of Directors; to subscribe and deliver all proper contracts of insurance; to take any action in furtherance of the exchange of such contracts of insurance; to do and perform every other thing that I could do in respect to such contracts so exchanged, including the appearance – and defense in my name in actions and proceedings; and to manage and conduct the business, affairs and property of the Exchange under the supervision of the Board of Directors.

2. The powers hereby vested in my said attorney shall be exercised only in accord with the decisions of the Board of Directors of the Association, provided that the

said attorney may deputize such person or persons as may be appointed therefore by the Board of Directors of the Association to authenticate the policy contracts now applied for or these that I may hereafter apply for, and all papers pertaining thereto. It is understood that the subscribers reserve unto themselves the right to govern the Association according to the decision of a majority of subscribers present in person or by proxy at any meeting.

3. I adopt as a part of this agreement the Bylaws of the Exchange now or hereafter effective.

4. I agree that this Power of Attorney shall have application to all insurance applied for by me, including such modifications or changes in any of my insurance as may be made at my request, and the representations made by me in connection with each policy shall have the same force and effect as if contained in this instrument.

5. I agree that, no director of United Services Automobile Association ("USAA") shall be personally liable to USAA or its members for monetary damages for any act or omission in the director's capacity as a director occurring from and after the adoption hereof, except in the following instances: (i) for any breach of the director's duty of loyalty to USAA or its members; (ii) for any act or omission not in good faith or which involves intentional misconduct or knowing violation of their law; (iii) for any transaction from which the director received an improper benefit, whether or not the benefit resulted from action taken with the scope of the director's office; (iv) for any act or omission for which the liability of a director is expressly provided for by statute; or (v) for any act

related to an unlawful stock repurchase or payment of a dividend.

6. I agree further that this Power of Attorney shall be and become effective on the date hereof and shall remaining [sic] force and effect only so long as I have a contract of insurance with the Exchange. This agreement is strictly limited to the use and the purpose herein expressed and to no other purpose.

Executed this _____ day of _____

19___, at _____.

Membership No. _____ SIGN HERE _____
(Do not print-legal signature required)

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**EXHIBIT C**

1ST CASE of Level 1 printed in FULL format. GARY NEIL, Plaintiff V. UNITED SERVICES AUTOMOBILE ASSOCIATION, Defendant and Third-Party Plaintiff V. DEARBORN AUTO, INC., ET AL., Third-Party Defendants

Civil Action 83-2414-MA

UNITED STATES DISTRICT COURT DISTRICT OF MASSACHUSETTS

Slip Opinion

February 15, 1984

COUNSEL:

George f. [sic] gormley, [sic] esq., [sic] One Center Plaza, Boston, MA 02108, for Plaintiff

Gerald Blair, Avery, Dooley, Post & Avery, 141 Tremont St., Boston, Ma. 02111, FOR DEARBORN AUTO, Philip J. McCarthy, Esq., LAW OFFICES OF PHILIP J. MCCARTHY, One Liberty Square, Boston, Mass. 02109, FOR CREATIVE COACH WORKS, INC., John A. Maloney, Esq., LAW OFFICES OF LEONARD N. AUGELLO, 10 Post Office Square, Suite 1155, Boston, Mass. 02109, for Defendant

OPINIONBY: [sic] MAZZONE

OPINION:

MEMORANDUM AND ORDER

MAZZONE, D.J.

Again, this matter is before the Court, this time on the defendant's motion to dismiss for lack of jurisdiction over the subject matter. Fed.R.Civ.P. 12(b)(1). The factual background of the dispute is set out fully in my Memorandum and Order of September 30, 1983. The plaintiff, a citizen of Massachusetts, asserted jurisdiction founded on diversity of citizenship.28 U.S.C. § 1332. In its present motion, the defendant claims that its legal status for purposes of establishing diversity of citizenship is that of an inter-insurance exchange association, and not a corporation. As such, the defendant claims its citizenship is determined by that of each of its members. There being a common citizenship between the plaintiff and thousands of the defendant's other members, the defendant moves this Court to dismiss for lack of jurisdiction.

The defendant is a reciprocal inter-insurance exchange. As cogently established by the Second Circuit in Baer v. United Services Automobile Association, 503

F.2d 393 (2d Cir. 1974), the defendant is an unincorporated association formed under Texas law and can not be considered a "corporation" for purposes of established diversity of citizenship. Citing Rosendale v. Phillips, 87 F.2d 454 (2d Cir. 1937) (per curiam), the Second Circuit noted: "For the purpose of the determining whether diversity of citizenship exists, unincorporated associations have long been considered to be citizens of each and every state in which the association has members. Thus, if the unincorporated association party to a lawsuit has any member whose state citizenship coincides with the state citizenship of any of the opposing parties in the lawsuit, a federal district court has no diversity jurisdiction."

The Second Circuit also noted that under United Steelworkers v. R.H. Bouligny, Inc., 382 U.S. 145 (1965), the formal distinction between the insurance reciprocal and the insurance corporation is dispositive on the issue of whether the reciprocal should be considered a corporation for diversity purposes, irrespective of whether the distinction is, as a practical matter, an artificial or illogical one. 503 F.2d at 395. The Second Circuit further commented that any trend toward erosion of the rule creating multiple state citizenship for unincorporated associations seems to have been halted abruptly by Bouligny. The Supreme Court in Bouligny acknowledged the significant similarity between corporations and certain other types of associations, but was unwilling to tamper with the existing statutory rule of 28 U.S.C. § 1332(c), which by its express terms applies only to corporations: "We are of the view that these arguments, however appealing, are addressed to an inappropriate forum, and that pleas for

extension of the diversity jurisdiction to nitherto [sic] uncovered broad categories of litigants ought to be made to the Congress and not to the courts." 382 U.S. at 150-51.

In view of the clear pronouncement of the Supreme Court in Bouligny, and the Second Circuit's cogent application of the law to this particular defendant in Baer, this Court finds the defendant to be an unincorporated association for the purposes of establishing diversity of citizenship. I cannot be persuaded by the plaintiff's attempts to enlarge the scope of 28 U.S.C. § 1332(c) to consider the defendant a corporation for jurisdictional purposes. There being no evidence to dispute the defendant's averment that it has thousands of members residing in Massachusetts, this Court must find that there is no diversity of citizenship between the plaintiff and the defendant. Accordingly, the complaint against the defendant must be dismissed.

In so doing, however, I must comment that it would behoove the defendant to act promptly and consistently in challenging diversity jurisdiction over it in Federal court actions. In the past, the defendant has both sued and allowed itself to be sued in Federal Court where jurisdiction was founded on diversity of citizenship, without challenging jurisdiction as it does in this present motion. See Feliciano v. United Services Automobile Association, 646 F.2d 695 (1st Cir. 1981); United Services Automobile Association v. Glens Falls Insurance Company, 429 F.Supp. 101 (D.Conn. 1976); United Services Automobile Association v. Middleton, 77 F.R.D. 660 (N.D.Ga. 1978). Selective challenges to jurisdiction bespeak a self-serving abuse of the Federal court processes. Such tactics are particularly odious since subject

matter jurisidiction is not a matter that can be created by laches, waiver or estoppel. See Owen Equipment & Erection Co. v. Kroger, 437 U.S. 365, 377 n.21 (1978); Page v. Wright, 116 F.2d 449 (7th Cir. 1940). Had the defendant acted promptly in challenging jurisdiction, substantial expense and effort to the plaintiff, as well as to the third-party defendants, would have been avoided.

Finally, because the defendant/third-party plaintiff was not properly subject to this Court's jurisdiction, the defendant/third-party plaintiff's complaint must also be dismissed as having been brought without this Court's jurisdiction. Fed.R.Civ.P. 14(a).

SO ORDERED.

ORDER OF DISMISSAL

MAZZONE, D.J.

In accordance with the Court's memorandum and order dated February 15, 1984 allowing the defendant's motion to dismiss, it is hereby ORDERED that the above entitled action and third party action be and hereby is dismissed.

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PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On JAN. 8 1992, I served the foregoing document described as:

PLAINTIFFS' SUPPLEMENTAL REPLY MEMORANDUM OF POINTS AND AUTHORITIES RE: OPPOSITION TO MOTION TO DISMISS

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [X] a true copy thereof enclosed in sealed envelopes addressed as follows:

Paul R. Fine, Esq.
Daniels, Baratta & Fine
1801 Century Park East
Ninth Floor
Los Angeles, California
90067
(213) 556-7900
FAX: (213) 556-2807

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE
ASSOCIATION

[COURTESY COPY FEDERAL EXPRESSED TO JUDGE WM. FREMMING NIELSEN]

---

[ ] BY MAIL

I caused such envelope to be deposited in the mail at Claremont, California. The envelope was mailed with postage thereon fully prepaid. I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal service

on that same day in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date deposit for mailing in affidavit.

[X] BY PERSONAL SERVICE

I caused to be delivered by hand to the above-listed addressees or to the addressees on the list attached hereto.

[ ] BY OVERNIGHT MAIL/COURIER

To expedite the delivery of the above-named document, said document was sent via overnight courier for next day delivery to:

[ ] BY FACSIMILE ("FAX")

In addition to the manner of proof of service indicated above, a copy was sent by FAX to:

[ ] (State) I declare under penalty of perjury under the laws of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Executed on JAN. 8 1992, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

**EXHIBIT A**

IN THE UNITED STATES DISTRICT COURT FOR THE MIDDLE DISTRICT OF GEORGIA, ALBANY-AMERICUS DIVISION

| | |
|---|---|
| HENRY A. PRIDGEN, As Next Friend for HENRY A. PRIDGEN, III, A Minor, Plaintiff, vs. UNITED SERVICES AUTOMOBILE ASSOCIATION, Defendant. | CIVIL ACTION NO. 84-247-ALB-AMER DEFENDANT'S BRIEF IN OPPOSITION TO PLAINTIFF'S MOTION TO REMAND |

I.

FACTUAL BACKGROUND

U.S.A.A., Defendant in the above action, is a reciprocal interinsurance exchange, domiciled in the State of Texas, and licensed under Chapter 19 of the Texas Insurance Code. U.S.A.A. is licensed to do business as a property/casualty insurer in all fifty states, as well as certain foreign locations, and has over 1.2 million policyholders. (Affidavit of John L. Swyers.)

U.S.A.A. is managed by a Board of Directors, elected by the policyholders at an annual meeting. Operational management is by a President, who is also the Attorney-in-Fact, and several Vice Presidents. The Association's headquarters are located in San Antonio, Texas in its own building which houses approximately 5,800 employees. Approximately 800 employees are located in field service offices in several other states.

U.S.A.A. is the parent company in an insurance holding company system regulated under Article 21.49-1 of the Texas Insurance Code. U.S.A.A. owns all the stock of several subsidiary Texas insurance and financial service corporations.

Upon being served by Plaintiff in Crisp County Superior Court for alleged failure to timely pay $47,500.00 in Personal Injury Protection benefits, U.S.A.A. removed this action to this Court pursuant to 28 U.S.C. § 1332. Plaintiff has filed his Motion to Remand.

II.

ARGUMENT AND CITATION OF AUTHORITY

(A)

For purpose of 28 U.S.C. § 1332, U.S.A.A. should be considered a citizen of Texas.

The U.S. Supreme Court in *Puerto Rico v. Russell & Co.*, 28 U.S. 476, 77 L.Ed. 903 (1933) the Court held in determining whether diversity of citizenship exists so as to give a Federal Court jurisdiction of a suit against a sociedad en comondita (sic) organized under Puerto Rican Commercial Code, the citizenship of its members is immaterial.

The Court said:

> "The petitioner argues, nevertheless, that the suit was not removable because of citizenship for the reason that the sociedad is a juridical entity under Puerto Rican law and, as in the case of a corporation, its domicil [sic] rather

than that of its members determines citizenship for purposes of federal jurisdiction."

"Therefore, to call the sociedad en comandita a limited partnership in the common law sense, as the respondents and others have done, is to invoke a false analogy. In the law of its creation the sociedad is consistently regarded as a juridical person. It may contract, own property and transact business, sue and be sued in its own name and right."

"Its members are not thought to have a sufficient personal interest in a suit brought against the entity to entitle them to intervene as parties defendant. See People v. Zayas, 29 P.R.R. 423, 430. It is created by articles of association filed as public records. Code of Commerce, § 95, 98; compare Civil Code § 1558, 1560. Where the articles so provide, the sociedad endures for a period prescribed by them regardless of the death of withdrawal of individual members. Civil Code § 1591, 1596, 1598, Code of Commerce § 141. Powers or management may be vested in managers designated by the articles from among the members whose participation is unlimited and they alone may perform acts legally binding on the sociedad. Civil Code § 1583, 1589; Code of Commerce § 102, 106, 125. Its members are not primarily liable for its acts and debts (Code of Commerce § 156), and its creditors are preferred with respect to its assets and property over the creditors of individual members, although the latter may reach the interests of the individual members in the common capital. Civil Code § 1590; see *Quintana Bros. & Co. v. S. Ramirez & Co.*, 22 P.R.R. 707, 716. Although the members whose participation is

unlimited are made contingently liable for the debts of the sociedad in the event that its assets are insufficient to satisfy them (Code of Commerce, § 125, 156; see *M. Lamadrid & Co. v. Torrens, M. & Co.*, 28 P.R.R. 824), this liability is of no more consequence for present purposes than that imposed on corporate stockholders by the statutes of some state." *Puerto Rico v. Russell & Co.*, 288 U.S. 476, 77 L. Ed. 903 (1933).

Further, *Moore's Federal Practice*, Volume 3, shows:

to unincorporated associations. The issue was thus framed: Did Congress intend, following Judge Learned Hand's underlying 'entity' theory, that unincorporated associations would not also have residence wherever, by analogy to corporations, they could be found to be doing business? Or on the other hand, did Congress, by its silence, merely adopt that narrow ruling in the *Sperry Products* case that unincorporated associations were residents of their 'principal palce [sic]' of business and stop with that? In a variety of contexts, some lower courts ruled that unincorporated associations were, analogous to corporations, residents wherever doing business, but others ruled they were residents only of their principal place of business.

In 1967, the Supreme Court ruled on the question in *Denver & Rio Grande Western R.R. Co. v. Brotherhood of Railroad Trainmen*. Adopting the theory that Congress had left the matter open for judicial development, the Court held that for venue purposes, unincorporated associations are to be assimilated to corporations and are to be considered residents wherever they are doing business. As an alternative holding, the Court found the 1966 amdndment [sic] of 28 U.S.C.

§ 1391(b), providing that suits can also be brought in the district 'in which the claim arose,' was applicable to the pending suit."

In *American Federation of Musicians v. Stein*, 213 F. 2d 679 (6th Cir.) the Court held:

"The description of the attributes of the United Mine Workers of America, as related by Chief Justice Taft, may, upon the trial of the instant case, be found equally applicable to the American Federation of Musicians. Whether in the light of People of Puerto Rico v. Russell & Co., supra, such national unions, with unity of action and power centered in their governing executive bodies, may be considered by the Supreme Court to be juridical persons equivalent to corporations for purposes of citizenship in cases in which jurisdiction is founded upon diversity of citizenship, is a question which, as far as this proceeding is concerned, is properly, in the first instance, subject to the consideration of the district court, where its determination, by virtue of the order of the court granting the preliminary injunction, abides the hearing.

Perhaps the most recent case in which the question has been determined is in *Van Sant v. American Express Co.*, 3 Cir., 169 F.ed (sic) 355, 372, where a New York joint stock association was treated as a corporation for purposes of diversity and, hence, as a citizen of New York. In its opinion, the court observed (in a footnote) that the old rule 'that generally speaking an unincorporated association has no citizenship for diversity purposes is itself beginning to show signs of being outmoded.' "

> However, the rule that the citizenship of unincorporated associations generally is that of its members, seems to be losing its vitality. 'There is some evidence . . . that the present federal rule is undergoing change, for the Supreme Court has treated a sociedad en comandita organized under Puerto Rico law as a citizen and resident of Puerto Rico for purposes of federal jurisdiction.' *Moore's Federal Practice*, Volume 3, page 1413 (2d Edition). In the case above referred to, *People of Puerto Rico v. Russell & Co.*, 288 U.S. 476, 53 S.Ct. 447, 448, 77 L. Ed. 903, the court held that a sociedad en comandita under the laws of Puerto Rico was not a limited partnership in the common-law sense, but a juridical person, with a personality like that of a corporation, and that it had the status of a corporation for purposes of federal jurisdiction, that is, citizenship."

The citizenship of a business trust is determined by the citizenship of the trustees, rather than that of the individual beneficiaries. *Navarro Savings Assoc. v. Lee*, U.S. 458 (1980).

U.S.A.A. is a "reciprocal inter-insurahce [sic] exchange" organized under the laws of the State of Texas. Under Texas Law, such exchanges are similar, if not identical to, corporations. In Wilson v. Marshall, 218 S.W. 2d 345, 346, (1949) the Court of Civil Appeals of Texas described them as follows:

> "The Subscribers at a reciprocal exchange are not only policyholders thereat and as such entitled to the protection afforded by the policies and required to pay the premiums stipulated in the policies; but they also own the

> insurance business just as stockholders own their corporation. They are the owners of their insurance exchange, and as such are entitled to reap the profits accruing from the operation of their insurance business and are also required to pay their pro rata part of the losses and expenses incurred at the exchange. It is their liability to pay their pro rata part of the losses and expenses that take the place of the capital structure of the exchange. When called upon to pay an assessment for his pro rata part of the losses, the subscriber at the exchange stands in the position of a stockholder in a stock insurance company whose capital structure has become depleted and who is required to pay a certain amount on each share of stock he owns into the coffers of the company to remove the deficit."

Additionally, indicia of the defendant's corporate status may be found in the fact that U.S.A.A. is the parent company in an insurance holding company system regulated under Article 21.49-1 of the Texas Insurance Code. U.S.A.A. owns all the stock of several subsidiary Texas insurance and financial service corporations. Also, like a corporation, U.S.A.A. is controlled by a Board of Directors, has officers, and is governed by a set of by-laws.

An examination of the Texas statutes pertaining to reciprocal inter-insurance exchanges indicates that such exchanges may be corporations. In fact, such an examination reveals that the term "reciprocal exchange" is less a description of the type of business organization than it is a description of the type of insurance arrangement. See Article 19.01 of the Texas Code of Insurance, a copy of which is attached to Mr. Swyers' affidavit.

Moreover, reciprocal insurance exchanges are subject virtually to the same regulatory scheme as corporations. See Article 19 of the Texas Insurance Code.

Additionally, United Services Automobile Association, has registered as a member of a holding company system under the Article 21.49-1 of the Texas Insurance Code, a statute generally regarded as governing corporate activity. See *Labowitz L.J. Corporations*, 26 Southwest Law Journal 87, 90, wherein said statute is discussed under the annual survey of corporate law. U.S.A.A.'s position in the holding system is as the parent or holding company, not simply as a small subsidiary, in the United Services Automobile Association group. Because U.S.A.A. is the parent company of a number of subsidiary corporations, and because, regardless of which subsidiary one is in fact dealing with, all communications are directed to the same corporate headquarters in San Antonio, Texas, one can conclude that the parent and the subsidiaries are really one and the same and should be treated as one corporation.

Clearly, U.S.A.A. is a corporate entity in everything but name. For this reason, Defendant urges this Court to treat it as such for purposes of determining its citizenship, as the Supreme Court did in *Puerto Rico vs. Russell & Company*, 288 U.S. 476 (1933). In that case the Court held that because a "sociedad decomandita" so closely resembled a corporation it should be treated as one for purposes of determining its citizenship. I so finding, the Court held that because the "socieded" is treated as a "judicial person" under the laws of Puerto Rico, "we saw no adequate reason in holding that the sociedad has a different status for purposes of federal jurisdiction than a

corporation organized under that law." So too, because U.S.A.A. appears to act and be treated as a "person distinct from its members", under the law of Texas, it should not be treated here any differently than a Texas corporation.

Plaintiff has relied in its Brief upon *Baer vs. United Services Automobile Association* 503 F.2d 393 (2d Cir. 1974), in which the Court of Appeals for the Second Circuit find sua sports, and parties were unable to bring most of the facts relied upon herein to the Court's attention. The decision appeared to rest exclusively upon the Court's reading of Articles 2 and (illegible) of the Texas Insurance Code, and the fact that U.S.A.A. restricts the availability of its insurance to servicemen. The Court apparently relied upon no Texas case law to reach its conclusion that a reciprocal exchange is not similar to a corporation. As mentioned above, *Wilson*, supra, holds that the two are almost identical. Nor did the Court consider U.S.A.A.'s status as a holding company, under Article 21.49-1 of the Texas Insurance Code. Lastly, *Baer* was decided in 1974, and, while it may have been a smaller operation then, which more closely resembled a voluntary association, today it is clearly, a huge corporate organization.

In *United Services Automobile Association vs. Glens Falls Insurance Company*, 429 F. Supp. 101, 105 (D. Conn. 1976) the Court described United Services Automobile Association as a "Texas corporation", and found diversity jurisdiction on that basis. That was a case in the Second Circuit decided two years after the *Baer* decision.

It is interesting to note that:

> "Business entities that are not incorporated pursuant to state law may qualify for treatment as corporations for federal tax purposes. These organizations called associations, must have more corporate characteristics than partnership or trust characteristics. The Treasury Regulations identify certain characteristics that establish 'corporateness' against which unincorporated business entities are measured. If the organization has more corporate characteristics than not, it will be identified as a corporation. These characteristics are: '(i) Associates, (ii) an objective to carry on business and divide the gains therefrom, (iii) continuity of life, (iv) centralization of management, (v) liability for corporate debts limited to corporate property, and (vi) free transferability of interests.'" *3A Cavitch, Business Organizations,* § 64.02(3).

Under 28 U.S.C. 1332, a corporation is a citizen of both the place of its incorporation and its principal place of business. United Services Automobile Association is, therefore, a citizen of Texas since it was organized under Texas law, and as a holding company, its principal place of business is considered to be the location of its "nerve center", i.e. "the location from which the corporation's officers direct, control, and coordinate all activities without regard to location, in the furtherance of the corporation objective" *Lugo Vina vs. Pueblo Intern Insurance,* 574 F.2d 41, 43, (1st Cir. 1979). Since all officer operate out of San Antonio, Texas, that is the "nerve center" and principal place of business of United Services Automobile Association.

For the foregoing reasons, the Defendant respectfully urges this Court to deny the Plaintiff's Motion to Remand.

(B)

Plaintiff contends this is a "direct" action against an insurance company and therefore is not removable pursuant to a proviso added to 28 U.S.C. § 1332: "Any direct action against the insuror [sic] of a policy or contract of liability insurance . . . such insuror shall be deemed a citizen of the State by which the insuror has been incorporated and of the State where it has its principal place of business."

It is basic hornbook law that removal jurisdiction is keyed to original diversity jurisdiction under 28 U.S.A. § 1332. "As under the predecessor statute, removal under section 1441 is keyed generally to original jurisdiction of the district of courts." 7B J. Moore, *Moore's Federal Practice*, at page J.C.-699.

Georgia's no-fault law in [sic] not a direct action statute. A direct action statute is one such as exists in Louisiana which permits the injured party to sue the tortfeasor's insurance company directly as opposed to having to sue the tortfeasor. (illegible) no stretch of the imagination is Georgia's no-fault law a direct action statute and no decision of the Georgia Courts has ever intimated as such. The Georgia no-fault law does not give an injured party any right to sue the liability carrier for the alleged tortfeasor. Instead, Georgia no-fault law merely provides a method for which an insured may collect benefits from its own insurance carrier and has nothing

to do with the alleged tortfeasor. A number of the cases cited by the Plaintiff at page 5 of its Brief are not in point with the instant case. For example, the *Hernandez* decision is one involving a workers' compensation claim. Workers' compensation claims are specifical [sic] excluded from removability pursuant to 28 U.S.C. § 1445(c). The *make-over* in this one *makeover* case was one involving a declarate judgment action by an insuror over a coverage issue and the court held that such actions do not come within the proviso in 28 U.S.C. § 1445(c). Finally, the *Azalea Meats, Inc.* case was one wherein a Georgia plaintiff (livestock seller) sued a number of parties when he had delivered some livestock and had not received payment. The party defendants included a number of Georgia parties, including the Commissioner of Agriculture and the insuror for the Commissioner of Agriculture. In an effort to cure the obvious defect in diversity jurisdiction, the plaintiff dismissed all Georgia defendants except the insuror for the Commissioner of Agriculture. The action was dismissed due to lack of jurisdiction and at pages 510 and 511, the Court emphasises [sic] that had it not done so, one could circumvent the purpose of proviso in subsection 'c' merely by filing suit against some resident defendants enjoining in a diverse insurance carrier and then later dismissing all but the insurance carrier. The factual situation presented by *Azalea Meats, Inc.* is not present in the instant case.

It cannot be overemphasized that in the instant case we do not have the situation where a plaintiff is suing the insurance carrier for an alleged tortfeasor and just has failed to join with the insured. In the instant case, the Plaintiff himself is the insured. Finally, contrary to the

assertions in Plaintiff rief, [sic] there is no "trend", especially to this circuit, to make the no-fault law into a direct action statute. The entire theory behind a direct action statute is that a thrid party who has been injured by an alleged tortfeasor, may sue the insuror for the alleged tortfeasor without joining the alleged tortfeasor (insured).

III.

CONCLUSION

We submit that the well reasoned decisions embraced in this Brief support the removal of this action.

Respectfully submitted,

BURT, BURT & DAVIS, P.A.

BY: /s/ Hilliard P. Burt
HILLIARD P. BURT,
Attorney for Defendant.

Post Office Box 525
Albany, Georgia 31703
(912) 432-6205

and

BY: /s/ C. Nathan Davis
C. NATHAN DAVIS,
Attorney for Defendant.

Post Office Box 525
Albany, Georgia 31703
(912) 432-6205

STATE OF GEORGIA,
COUNTY OF DOUGHERTY.

CERTIFICATE OF SERVICE

This will certify I have this date served upon opposing counsel of record, JOHN C. PRIDGEN, P. O. Box 397, Vienna, Georgia 31092, a copy of the above and foregoing "Defendant's Brief In Opposition To Plaintiff's Motion To Remand" by depositing said copy in the United States Mail, addressed as written above, with sufficient postage thereon to insure proper delivery of same.

This the 29th day of November, 1984.

BURT, BURT & DAVIS, P.A.

BY: /s/ Hilliard P. Burt
HILLIARD P. BURT,
Attorney for Defendant.

Post Office Box 525
Albany, Georgia 31703
(912) 432-6205

---

**EXHIBIT A**

AFFIDAVIT

STATE OF TEXAS :

COUNTY OF BEXAR :

Before me, the undersigned authority, on this day personally appeared JOHN L. SWYERS, known to me, and being first duly sworn, desposes and states the following, to wit:

I am JOHN L. SWYERS, of lawful age, residing in the State of Texas. I am employed by United Services Automobile Association as Vice President-Associate General Counsel/Assistant Secretary.

In the above-stated capacity, I affirm that United Services Automobile Association (USAA) is a reciprocal interinsurance exchange, domiciled in Texas, and licensed under chapter 19 of the Texas Insurance Code. USAA is licensed to do business as a property/casualty insurer in all fifty states, as well as certain foreign locations, and has over 1.2 million policyholders.

As a reciprocal, USAA is owned by its policyholders who, through their premiums, contribute the necessary capital. Profits are returned to the policy holders through policy dividends and allocations to Subscriber's Savings Accounts (said allocated funds are paid to the policyholder whenever he or she terminates all policies). Operationally, USAA can be said to function much like a mutual insurer.

USAA is managed by a Board of Directors, elected by the policyholders at an annual meeting. Operational management is by a President, who is also the Attorney-in-Fact, and several Vice Presidents. The Association's headquarters are located in San Antonio, Texas in its own building which houses approximately 5800 employees. Approximately 800 employees are located in field service offices in several other states.

USAA is the parent company in an insurance holding company system regulated under Article 21.49-1 of the

Texas Insurance Code. USAA owns all the stock of several subsidiary Texas insurance and financial service corporations.

Attached hereto are copies of Chapter 19 and Article 21.49-1 of the Texas Insurance Code. Also attached is a pamphlet entitled "USAA Bylaws" which I certify to be a true and correct copy of the Associaiton's [sic] current Bylaws.

The undersigned is competent to make this Affidavit and understands it will be used as evidence in the case of HENRY A. PRIDGEN, As Next Friend for HENRY A. PRIDGEN, III, A Minor vs. U.S.A.A.; U.S. District Court No. 84-247-ALB-AMER, Middle District of Georgia.

/s/ John L. Swyers
JOHN L. SWYERS

Subscribed and sworn to before me this 27th day of November 1984.

/s/ Loretta C. Lanicek
LORETTA C. LANICEK
Notary Public
Bexar County, Texas

My commission expires 11/30/88

---

**EXHIBIT B**

AFFIDAVIT OF BILL SOUZA

BILL SOUZA, being first duly sworn on oath, deposes and says that:

1. I am the Assistant Vice President and Claims Manager of Hawaiian Insurance and Guaranty Company, Ltd., a Hawaii Corporation.

2. I hereby certify that we have paid United Services Automobile Association $391,343.50, pursuant to a Judgment and an Order rendered in CA No. 88-2941, CV-84-0300-ACK and CV-87-0483-ACK (consolidated).

FURTHER AFFIANT SAYETH NAUGHT

/s/ Bill Souza
BILL SOUZA

subscribed and sworn before me this
7th day of November, 1991.

/s/ illegible (Seal)
Notary Public, State of Hawaii

My commission expires: 12-9-91

**Hawaiian Insurance Group**
**[HEI]**

**[LOGO]**

1001 Bishop Street
Bishop Square •
Pacific Tower
Honolulu, HI 96813-3429
Phone (808) 536-2777

Mailing Address:
Post Office Box 2255
Honolulu, HI 96804-2255

FAX (808) 547-8398
Cable Hawguar/
Telex 671-1835
Answer Back HIC-UW

November 25, 1991

Mr. William M. Shernoff
Shernoff, Bidart & Darras
600 South Indian Hill Blvd.
Claremont, CA 91711-5498

Re: **Waters v. USAA**

Dear Mr. Shernoff:

In our situation, ***USAA v. HIG***, we issued three(3) payments to USA.

The first was on 12/19/89, for $353,417.88. The second was on 3/8/90, for $37,549.20. The final was on 4/13/90, for $376.42.

Thank you.

Very truly yours,

/s/ Bill Souza
Bill Souza
Assistant Vice President

FWS/ei

cc: Walt Davis
Law Offices of Ian L. Mattoch
Suite 1835, Grosvenor Center
737 Bishop Street
Honolulu, HI 96813

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**EXHIBIT C**

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**LOCAL NEWS/WEATHER/EDITORIAL PAGES**

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**METRO**

FRIDAY
NOVEMBER 8, 1991 *Los Angeles Times*

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## Insurance Firm Flip-Flopped in Claims Cases

■ **Legal system:** USAA has history of arguing on both sides of the fence about courts' jurisdiction regarding non-payment claims. Sanctions of $1.7 million sought.

By HENRY WEINSTEIN
TIMES STAFF WRITER

United Services Automobile Assn., one of the nation's largest insurance companies, has for years argued on both sides of the fence about whether suits against it for non-payment of claims should be argued in state or federal court.

In more than 170 instances throughout the United States, the Texas-based company has argued to both federal and state judges that it was being sued in the wrong

court, failing to reveal that it had argued the other way in other cases, frequently simultaneously.

Now, in a case involving a federal judge in Los Angeles whose home was severely damaged in a fire, this chameleon-like behavior is being challenged as fraudulent ducking of legitimate claims.

U.S. District Court Judge Laughlin E. Waters is asking that USAA pay him and his wife sanctions of $1.7 million for engaging "in a massive, widespread and fraudulent scheme to mislead the federal courts and to manipulate federal court jurisdiction to suit its own purposes."

Court records show that during the past two decades, USAA, attempting to avoid paying claims, has repeatedly given different descriptions of what kind of company it is. These contentions were a critical element as lawyers for the company argued that cases should be heard in federal or state court depending on what appeared to serve its best interests.

The sanctions issue, scheduled for a hearing today, stems from a suit filed in federal court here last July by Waters, a federal judge since 1976, and his wife, Voula. The Waters allege that USAA acted in bad faith, stonewalling them when they filed an insurance claim after their Hancock Park home burned last December.

Their suit states that there is federal jurisdiction because they are California residents and USAA is a Texas corporation. USAA has moved to have the suit dismissed. The company claims that it is an unincorporated association with 280,000 members in California – its

policyholders – and therefore the case does not belong in federal court.

But the Waters, represented by Claremont attorney William M. Shernoff, responded by citing 172 instances where USAA has taken contradictory positions on its corporate status.

"USAA's pattern of deliberate abuse of the federal courts is probably the most widespread, nefarious scheme perpetrated on the federal courts in the history of the federal judiciary." Shernoff asserted in a brief "USAA argues it is a corporation or corporate like entity when it suits USAA to be in federal court, and argues it is an unincorporated association when it suits USAA to get out of federal court."

The company, in court documents, acknowledged that its attorneys have made conflicting statements.

But Timothy B. Dyk, a Washington lawyer, denied that USAA had acted in bad faith, saying the company had thousands of cases in litigation and that it was difficult to keep track of what contentions were being made in each of them.

A brief filed for USAA by Century City lawyer Paul R. Fine contends that the company has done nothing wrong in the Waters case and that the court has no power to sanction USAA for anything that happened in a prior case.

However, several lawyers and law professors said they were deeply troubled by what USAA has done in these cases.

"You can't claim you're a fish in one court and a fowl in the other," said attorney Edward F. Silva, who had a suit against USAA in Philadelphia. "It's not honest to do that."

"This company is the 'Zelig' of federal jurisdiction," said New York University law professor Stephen Gillers, referring to the Woody Allen movie about a man who constantly changes his persona to suit his purposes.

Gillers, who specializes in legal ethics, reviewed the documents in the Waters case and said they show that the federal court system can be duped. "The company has manipulated its status so that no rule applies to it," he said.

Court records show that USAA's general counsel filed an affidavit in a Georgia federal court in 1984 supporting the company's bid to move a case from state court to federal court on jurisdictional grounds. But he filed another affidavit in a Washington case in 1987 supporting USAA's contention that there was no jurisdiction to sue it in federal court.

University of San Francisco law professor Jeffrey S. Brand, who specializes in federal litigation and *

He said this is the sort of situation that has prompted calls for reform of the nation's civil justice system.

"Conduct like this should be of great concern to everyone because it makes it impossible" for the legal system to function properly, Brand said.

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Brand and Gillers said they were not sure if the Waters are entitled to sanctions, but said some action was warranted based on USAA's pattern of conduct. Both said some individuals and companies who had opposed USAA in earlier cases might be entitled to have those cases reopened.

The issue is under consideration by U.S. District Judge Wm. Fremming Nielsen of Spokane, Wash. He was brought in to hear the suit when all the federal judges in Los Angeles had to disqualify themselves because of their relationship to Waters.

Founded in 1922, USAA is the nation's eighth-largest insurance company, with $5.6 billion in assets, an operating surplus of $2.7 billion and profits of $65 million last year, according to Best's Insurance Guide. The company insures only current and former members of the armed services and their families.

Last June, California Insurance Commissioner John Garamendi praised USAA for having the best record of consumer service on auto claims. He also said the agency did not find a single justified complaint against the company by a homeowner.

But Waters, 77, and his wife say they have had a very disturbing experience with USAA.

Last December, the couple's large, elaborately decorated residence on June Street suffered severe fire damage. A company chosen by the Waters made an estimate for repair work of $442, 663, court documents say.

During the next several months, repair companies chosen by USAA submitted considerably lower estimates,

starting at $116,587 and * restore the Waters' home, attorney Shernoff alleged in the suit.

When the two sides could not agree, Waters said he and his wife decided to sue.

Shernoff said the Waters' lives have been thrown into turmoil by USAA's intransigence, forcing them to rent a house for many months and leading to multiple hospitalizations of Mrs. Waters "for anxiety, stress and high blood pressure."

The issue of jurisdiction in USAA claims first arose in 1974. While defending a lawsuit in New York, USAA contended that it was not a corporation, but an "inter-insurance exchange," all of whose policyholders are members of the exchange. A federal appeals court ruled in USAA's favor, saying it could not be sued in a New York federal court, or a federal court in any other state where it has members. USAA is licensed to sell insurance in every state.

However, in the years since then USAA has continually flip-flopped on whether it should be in federal court, sometimes changing its mind in the same case.

For example, in 1984 it took sharply diverging positions in federal courts in Massachusetts and Georgia.

Gary Neil filed suit in federal court in Boston after USAA failed to pay a claim on his auto insurance. USAA waited several months, then challenged jurisdiction. Although U.S. District Judge A. David Mazzone agreed

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with USAA and dismissed the suit citing the 1974 Baer case, he chastised the * behoove the defendant to act promptly and consistently in challenging diversity jurisdiction over it in federal court actions," Judge Mazzone said in his February, 1984 decision. "In the past, the defendant has both sued and allowed itself to be sued in federal court where jurisdiction was founded on diversity of citizenship, without challenging jurisdiction as it does in this case."

"Selective challenges to jurisdiction bespeak a self-serving abuse of the federal court processes." Mazzone said.

Neil's lawyer, George F. Gormley, refiled the suit in state court and seven years later collected a $32,000 judgment against two other two defendants. A jury found USAA not liable. Gormley said he believed that USAA wanted the case out of federal court because Mazzone had made preliminary rulings favorable to Neil.

Just months after Mazzone's 1984 decision, USAA reversed direction in Georgia. Henry A. Pridgen had filed suit in Crisp County Superior Court alleging that the company had failed to pay him $47,500 in personal injury protection benefits. This time, USAA successfully got the case switched to federal court, arguing that Pridgen was a Georgian and USAA was "a citizen of Texas."

USAA lawyers contended that the 1974 Baer decision was outmoded.

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"While it [USAA] may have been a smaller operation then, which more closely resembled a voluntary association today it is * llard P. Burt. To support this contention in November, 1984, John L. Swyers, USAA's associate general counsel, signed an affidavit describing the company's status, which was attached to Burt's brief.

Attorney John C. Pridgen, who represented his cousin Henry in the case, said he believed USAA wanted to get out of the state court located in his cousin's hometown. He said the fact that USAA was able to invoke federal jurisdiction in this case while escaping it in others showed that persons suing the company weren't able to litigate on "a level playing field." The case was settled on the eve of trial.

The next major decision on USAA's status began in Tulsa, Okla., federal court in 1983. Leroy and Dorothy Tuck sued USAA, contending the company acted in bad faith when it failed to pay the couple's claims after their son Johnny, a Marine Corps helicopter pilot, was killed by a drunk driver. The federal jury awarded the Tucks $900,000, which a judge reduced to $675,000. On appeal, citing the Baer opinion, USAA asserted that the court had no jurisdiction.

But while the Tuck appeal was pending, USAA filed suits in federal courts in Birmingham, Ala., Philadelphia and San Diego Claiming it was a Texas corporation.

Changing direction again, the company filed a motion seeking to dismiss a case in Seattle federal court, buttressed by an affidavit from general counsel Swyers.

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In October, 1988, the 10th Circuit Court of Appeals ruled in USAA's favor in the Tuck case.

However, the appeals court noted that USAA had taken contradictory positions on jurisdiction. The judges said of USAA: "We expect to make similar motions" to get out of all its pending federal cases.

Four months later, Patrick E. Carr, the Tucks' lawyer, asked the 10th Circuit to impose sanctions on USAA because of its allegedly * sanctions motion asserting that despite the 10th Circuit's 1988 decision, USAA continued to appear in federal court in 22 cases. The Tucks received a $1.4 million settlement.

Additionally, attorney Dyk submitted a report to the court for USAA describing steps the company "has taken and is taking to insure that USAA . . . will not be a party to actions in federal courts based on diversity of citizenship."

The report said that USAA first advised all regional claims officials in May, 1988, to seek dismissal of all federal suits against it. The report said the company sent out another bulletin in December, 1988, advising its officials to "stay out of federal court."

Nonetheless, the company acknowledged, some federal cases remained open. One of those suits was filed in 1984 in Honolulu federal court by USAA against another insurance company. USAA prevailed at trial and on appeal.

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In successfully arguing the appeal in May, 1989, seven months after the 10th Circuit decision, USAA once again described itself as a Texas corporation. In December, 1989, USAA collected a $353,417 judgment from Hawaiian Insurance Group in the Honolulu case.

Bill Souza, Hawaiian Insurance Group vice president, said in an interview this week that he had just learned about the federal appeals court decision directing USAA to get out of federal court.

"I'm kind of floored by this," he said. "I feel these people did not act in good faith." Souza said he has asked the group's attorney to file papers seeking to have the judgment set aside and for USAA to be sanctioned.

USAA officials in San Antonio declined to answer questions about the controversy. Company spokesman Hal Schade issued a brief statement, saying USAA was following constitutional guidelines on *

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**'USAA's pattern of deliberate abuse of the federal courts is probably the most widespread, nefarious scheme perpetrated on the federal courts in the history of the federal judiciary.'**

---

WILLIAM M. SHERNOFF
*Attorney*

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## PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On DEC. 9 1991, I served the foregoing document described as:

PLAINTIFFS' SUPPLEMENTAL BRIEFING AS ORDERED BY COURT IN OPPOSITION TO MOTION TO DISMISS AND IN SUPPORT OF REQUEST FOR SANCTIONS

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [X] a true copy

thereof enclosed in sealed envelopes addressed as follows:

Paul R. Fine, Esq.
Daniels, Baratta & Fine
1801 Century Park East
Ninth Floor
Los Angeles, California
90067
(213) 556-7900
FAX: (213) 556-2807

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE
ASSOCIATION

---

[ ] BY MAIL

I caused such envelope to be deposited in the mail at Claremont, California. The envelope was mailed with postage thereon fully prepaid. I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal service on that same day in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date deposit for mailing in affidavit.

[X] BY PERSONAL SERVICE

I caused to be delivered by hand to the above-listed addressees or to the addressees on the list attached hereto.

[ ] BY OVERNIGHT MAIL/COURIER

To expedite the delivery of the above-named document, said document was sent via overnight courier for next day delivery to:

[ ] BY FACSIMILE ("FAX")

In addition to the manner of proof of service indicated above, a copy was sent by FAX to:

[ ] (State) I declare under penalty of perjury under the laws of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Executed on DEC. 9 1991, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

PAUL R. FINE, ESQ.
DANIELS, BARATTA & FINE
1801 Century Park East
Los Angeles, California 90067
(213) 556-7900

OF COUNSEL:

JONES, DAY, REAVIS & POGUE
1450 G STREET, N.W.
Washington, D.C. 20005
(202) 879-3939

Attorneys for Defendant UNITED SERVICES AUTOMOBILE ASSOCIATION

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br>Plaintiffs,<br>v.<br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br>Defendant. | Case No. CV-91-3615-WFN<br>NOTICE OF MOTION AND MOTION FOR CERTIFICATION PURSUANT TO 28 U.S.C. § 1292<br>(Filed Feb. 11, 1992)<br>(Judge Wm. Fremming Nielson)<br>Date: March 9, 1992<br>Time: 10:00 a.m.<br>Courtroom: To Be Announced<br>Trial Date: September 14, 1992 |

TO PLAINTIFFS LAUGHLIN E. WATERS AND VOULA D. WATERS AND TO THEIR ATTORNEYS OF RECORD HEREIN:

PLEASE TAKE NOTICE that on March 9, 1992, at 10:00 a.m., or as soon as the matter may be heard by Order of the Court, defendant, UNITED SERVICES AUTOMOBILE ASSOCIATION ("USAA"), will move the Court to rule that the Order filed on February 7, 1992 (the "Order"), which denied USAA's motion to dismiss for lack of subject matter jurisdiction, should be certified for immediate appeal pursuant to 28 U.S.C. § 1292(b).

This motion will be made on the grounds that the Order involves a controlling question of law as to which there is a substantial ground for difference of opinion, and that an immediate appeal from the Order may materially advance the ultimate termination of this litigation. In particular, the motion will argue that the Order obviously presents a controlling question of law since it presents the threshold question of whether this Court has subject matter jurisdiction. The motion will further argue that the Order's ruling that USAA should be deemed to be a corporation for purposes of diversity jurisdiction conflicts with the Supreme Court's instructions in *Carden v. Arkoma Assocs.*, 494 U.S. 185 (1990), for determining jurisdictional status, and that the Order expressly conflicts with decisions of the Second and Tenth Circuits which have held that USAA is deemed to be a citizen of every state in which it has members.

This motion will be based on this notice and the Memorandum in Support of Certification Pursuant to 28

U.S.C. § 1292(b), which is attached hereto and submitted herewith.

Dated: February 11, 1992

DANIELS, BARATTA & FINE

By: /s/ Paul R. Fine by DM
Paul R. Fine

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE ASSOCIATION

*Of Counsel*:

JONES, DAY, REAVIS & POGUE
1450 G Street, N.W.
Washington, D.C. 20005
(202) 879-3939

**VERIFICATION**

STATE OF CALIFORNIA, COUNTY OF

I have read the foregoing _____

_____ and know its contents

[X] CHECK APPLICABLE PARAGRAPH

[ ] I am a party to this action. The matters stated in the foregoing document are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

[ ] I am [ ] an Officer [ ] a partner _____ [ ]

a _____ of _____

_____

a party to this action, and am authorized to make this verification for and on its behalf, and I make this verification for that reason. [ ] I am informed and believe and on that ground allege that the matters stated in the foregoing document are true. [ ] The matters stated in the foregoing document are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

[ ] I am one of the attorneys for _____ , a party to this action. Such party is absent from the county of aforesaid where such attorneys have their offices, and I make this verification for and on behalf of that party for that reason. I am informed and believe and on that ground allege that the matters stated in the foregoing document are true.

Executed on _____, 19 _____, at _____, California.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

_____ _____

Type or Print Name Signature

**PROOF OF SERVICE**
1013A (3) CCP Revised 5/1/88

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles , State of California.

I am over the age of 18 and not a party to the within action; my business address is: 555 West 5th Street, Suite 4600, Los Angeles, California 90013

On 2/11/, 19 92. I served the foregoing document described as Notice of Motion And Motion For Certification Pursuant to 28 U.S.C. Section 1292

_____ on the interested parties in this action

[ ] by placing the true copies thereof enclosed in sealed envelopes addressed as stated on the attached mailing list:

[X] by placing [ ] the original [x] a true copy thereof enclosed in sealed envelopes addressed as follows:

Frank M. Darras, Esq.
William M. Shernoff, Esq.
Shernoff, Bidart & Darras
600 South Indian Hill Blvd.
Claremont, CA 91711-5498

[X] BY MAIL

[ ] *I deposited such envelope in the mail at

_____, California.

The envelope was mailed with postage thereon fully prepaid.

[X] As follows: I am "readily familiar" with the firm's practice of collection and processing correspondence for mailing.

Under that practice it would be deposited with U.S. postal service on that same day with postage thereon fully prepaid at Los Angeles California in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postag meter

date is more than one day after date of deposit for mailing in affidavit.

Executed on _____ , 19 _____, at

_____, California.

[ ] **(BY PERSONAL SERVICE) I delivered such envelope by hand to the offices of the addressee.

Executed on _____, 19 _____, at

_____, California.

[ ] (State) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Martha Espelage
Type or Print Name

/s/ Martha Espelage
Signature

PAUL R. FINE, ESQ.
DANIELS, BARATTA & FINE
1801 Century Park East
Los Angeles, California 90067
(213) 556-7900

OF COUNSEL:

JONES, DAY, REAVIS & POGUE
1450 G STREET, N.W.
Washington, D.C. 20005
(202) 879-3939

Attorneys for Defendant UNITED SERVICES AUTOMOBILE ASSOCIATION

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. CV-91-3615-WFN<br><br>MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT'S MOTION FOR CERTIFICATION PURSUANT TO 28 U.S.C. § 1292<br><br>(Filed Feb. 11, 1992)<br><br>(Judge Wm. Fremming Nielson)<br><br>Date: March 9, 1992<br>Time: 10:00 a.m.<br>Courtroom: To Be Announced<br>Trial Date: September 14, 1992 |

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UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

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| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br>Plaintiffs,<br>v.<br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br>Defendant. | Case No. 91 3615 WFN<br>MEMORANDUM IN SUPPORT OF DEFENDANT'S MOTION FOR CERTIFICATION PURSUANT TO 28 U.S.C. § 1292<br>(Judge Wm. Fremming Nielson)<br>Trial Date: September __, 1992 |

## INTRODUCTION

The February 7, 1992 Order (the "Order") entered by this Court denied a motion to dismiss for lack of subject matter jurisdiction and holds that this Court has jurisdiction because Defendant, UNITED SERVICES AUTOMOBILE ASSOCIATION ("USAA"), should be treated as a Texas corporation for diversity purposes. In doing so, USAA believes that the Order conflicts with the Supreme Court's decision in *Carden v. Arkoma Assocs.*, 494 U.S. 185 (1990), which held that the citizenship of an artificial entity other than a corporation should be measured by the citizenship of all of the entity's members. In addition, the Order concededly (Order at 5) creates a direct conflict with decisions by the Second and Tenth Circuits, both of which have held that USAA should be treated as an unincorporated association and that, since USAA has members in each state, it therefore cannot participate in

federal diversity litigation. Since subject matter jurisdiction cannot be waived, the Order raises the prospect that the parties and the Court will go through an entire trial of this action only to have the result discarded due to a subsequent holding that there was no subject matter jurisdiction. Moreover, as a practical matter, the conflicts created by the Order place USAA in the untenable position of being unable to determine whether it can properly litigate in federal diversity cases. In these circumstances, this Court should certify the Order for immediate appeal under 28 U.S.C. § 1292(b) (1988).

## ARGUMENT

Section 1292(b) allows for the immediate appeal of an order if the district court certifies that it:

> involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation.

28 U.S.C. § 1292(b).[1] Thus, as the Ninth Circuit held in *In re Cement Antitrust Litigation*, 673 F.2d 1020, 1026 (9th Cir. 1982), *aff'd for lack of quorum*, 459 U.S. 1190 (1983), there are three requirements that must be met before § 1292(b) certification is appropriate: "(1) that there be a controlling question of law, (2) that there be substantial grounds for difference of opinion, and (3) that an immediate appeal

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[1] Under § 1292(b), the district court's certification may be added to an existing order at any time through an amendment. *See* Fed. R. App. P. 5(a).

may materially advance the ultimate termination of the litigation." The Order satisfies each requirement. Indeed, it is the quintessential case for certification under § 1292(b).

## I. Since The Order Resolves A Threshold Jurisdictional Issue, It Clearly Presents A Controlling Question Of Law

Section 1292(b)'s first requirement – that the order involve a "controlling question of law" – is easily satisfied here. "[A]ll that must be shown in order for a question to be 'controlling' is that resolution of the issue on appeal could materially affect the outcome of litigation in the district court." *In re Cement Antitrust Litigation*, 673 F.2d at 1026. The issue resolved by the Order is whether this Court has subject matter jurisdiction over the lawsuit. There can hardly be an issue that more "materially" impacts the outcome of the litigation.

The Order itself notes that it was resolving "[t]he *key* issue [of] whether or not USAA is to be treated as a corporate or non-corporate entity." Order at 2 (emphasis added). Under *Carden*, this question of corporate or non-corporate characterization controls USAA's citizenship for diversity purposes. Corporate entities are deemed to be citizens only of their states of incorporation or of their principal places of business. 28 U.S.C. § 1332(c)(1) (1988). But *Carden* held that, "to determine, for diversity purposes, the citizenship of [a non-corporate] entity, the court [must] consult the citizenship of . . . all of the entity's members." 494 U.S. at 195. Since, as the Order

recognized (Order at 1), some USAA members are citizens of the same state as the Plaintiffs, the requisite complete diversity exists only if USAA is deemed to be corporate entity. Thus, in a very real sense, the Order involves a controlling question of law: if the Order's conclusion that USAA is a corporate entity is correct, then the suit can go forward in federal court; but if USAA must be treated as a non-corporate entity, then the entire case must be dismissed for lack of subject matter jurisdiction.

The courts and commentators consistently recognize that this type of jurisdictional determination is a "controlling question" for purposes of § 1292(b). As the Ninth Circuit explained in *United States v. Woodbury*, 263 F.2d 784, 787 (9th Cir. 1959) (emphasis added; footnotes omitted):

> Section 1292(b) was intended primarily as a means of expediting litigation by permitting appellate consideration during the early stages of litigation of legal questions which, if decided in favor of the appellant, would end the lawsuit. Examples of such questions are *those relating to jurisdiction* or a statute of limitations which the district court has decided in a manner which keeps the litigation alive but which, if answered differently on appeal, would terminate the case.

*Accord, In re Western Liquid Asphalt Cases*, 487 F.2d 202, 203-04 (9th Cir. 1973) (§ 1292(b) review of a district court order denying motion to dismiss for lack of subject matter jurisdiction), *rev'd on other grounds*, 419 U.S. 186 (1974). Other courts also have expressly recognized that the issue of subject matter jurisdiction is a controlling question and

thus is an appropriate candidate for § 1292(b) review. *See, e.g., Miche v. Great Lakes Steel Div.*, 495 F.2d 213, 214-15 (6th Cir.) (§ 1292(b) review of whether diversity jurisdiction was present), *cert. denied*, 419 U.S. 997 (1974); *Leaseco Data Processing Equip. Corp. v. Maxwell*, 468 F.2d 1326, 1330 (2d Cir. 1972) (§ 1292(b) review of issues of personal and subject matter jurisdiction).[2]

Indeed, the Sixth Circuit recently accepted for § 1292(b) review a case that is strikingly similar tc this one. In *SHR Limited Partnership v. Braun*, 888 F.2d 455 (6th Cir. 1989), the court considered a diversity suit brought by two West Virginia limited partnerships against several Michigan citizens. Many of the limited partners in the partnerships also were Michigan residents and, accordingly, the defendants moved to dismiss for lack of complete diversity. *Id.* at 456. The district court denied the motion to dismiss because it concluded that the limited partners need not be considered to determine the citizenship of the partnerships. *Id.* The defendants then moved for certification, and the district court granted the motion, finding that the jurisdictional issue "concerned a controlling issue of law upon which there is substantial ground for differences of opinion." *Id.* The Sixth Circuit

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[2] *See also* 9 J. Moore, B. Ward & J. Lucas, *Moore's Federal Practice* ¶ 110.22[2], at 268-70 & n.13 (2d ed. 1991) (noting that "a question as to jurisdiction of the subject matter" is a familiar example[] of controlling questions"); 16 C. Wright, A. Miller, E. Cooper & E. Gressman, *Federal Practice and Procedure* § 3930, at 158 (1977) (noting that "an initial question of jurisdiction" is an appropriate candidate for interlocutory review).

agreed, and accepted the appeal.[3] In the face of *SHR Limited Partnership v. Braun* and these other authorities, there can be no doubt that § 1292(b)'s first requirement is met here.

## II. There Is Substantial Ground For Difference Of Opinion As To The Jurisdictional Issue Resolved In The Order

Likewise, it is plain that § 1292(b)'s second requirement is easily satisfied in this case. Specifically, certification is appropriate here because the legal issue resolved in the Order plainly is one "as to which there is substantial ground for difference of opinion." 28 U.S.C. § 1292(b).

### A. There Is Substantial Reason To Believe That The Order Conflicts With The Supreme Court's Decision In Carden v. Arkoma Associates

In *Carden*, the Court held that the citizenship of the "wide assortment of artificial entities" that "[t]he 50 States have created, and will continue to create" must be measured by the citizenship of each of their members:

> In sum, we reject the contention that to determine, for diversity purposes, the citizenship of an artificial entity, the court may consult the citizenship of less than all of the entity's members. . . . [Rather,] a suit by or against the entity depends on the citizenship of all the members.

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[3] The Sixth Circuit went on to reverse, holding that the citizenship of the limited partnerships must be determined by reference to all of their members. 888 F.2d at 457-59.

*Id.* at 195-97 (quotation omitted). USAA believes that the Order's conclusion that USAA's citizenship is *not* that of its individual members conflicts directly with *Carden*.

The Order's sole basis for distinguishing *Carden* and holding that USAA should be deemed to be a corporation for diversity purposes is *Puerto Rico v. Russell & Co.*, 288 U.S. 476 (1933). *Russell* involved the issue of whether a case involving a sociedad en comandita, an entity organized under the civil code of Puerto Rico, could be removed from a Puerto Rican court to federal court. *Id.* at 477-78. Removal was permitted only if the sociedad was deemed to be a "citizen" not just of Puerto Rico, but of every state in which it had a member. *Id.* at 478-79. The Court held that the sociedad's citizenship should not be measured by that of its members; instead, the Court held that the sociedad should be viewed as a "juridical person" and thus as a citizen of Puerto Rico, under whose laws it was organized. *Id.* at 481.

The Order determines that because *Carden* did not overrule *Russell*, the functional analysis undertaken in *Russell* is appropriately applied to USAA. Thus, the Order holds that, because the characteristics of the sociedad en comandita are similar to certain characteristics of a reciprocal insurance exchange under Texas law, USAA should be treated as a "juridical person" just as the sociedad was in *Russell*. *See* Order at 4. USAA believes that this approach is flawed in three respects.

*First*, *Carden* made it clear that the functional approach to jurisdictional status used in *Russell* did not apply in other settings. USAA therefore believes that the

entire premise of the Order's analysis is flawed. Specifically, the Order compares various characteristics that the sociedad en comandita and a Texas reciprocal exchange share, and concludes that these similarities compel the conclusion that the two entities must be given the same jurisdictional treatment. *See* Order at 4. *Carden* expressly rejected not only this general approach to determining jurisdictional status, but this particular reading of *Russell* as well. In *Carden*, the Court addressed the respondent's argument that "th[e] language, and the outcome of [*Russell*] 'reflec[t] the Supreme Court's willingness to look beyond the incorporated/unincorporated dichotomy and to study the internal organization, state law requirements, management structure, and capacity or lack thereof to act and/or sue, to determine diversity of citizenship.' " 494 U.S. at 190. In other words, the respondent in *Carden* argued for precisely the same reading of *Russell* adopted by the Order. The *Carden* Court, however, quickly rejected such an analysis, ruling "that th[is] approach . . . was proposed and specifically rejected in [*United Steelworkers v.*] *Bouligny*[, 382 U.S. 145 (1965)]." 494 U.S. at 190. Thus, *Carden* and *Bouligny* completely foreclose the method of analysis, and the reading of *Russell*, adopted in the Order.[4]

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[4] It also should be noted that the same features that the Order points to in aligning a reciprocal exchange with the sociedad en comandita apply to limited partnerships and other types of unincorporated associations. Indeed, the dissent in *Carden* – which gave *Russell* the same type of broad reading as the Order – complained that a limited partnership was a "virtually identical stateside counterpart" to the sociedad en comandita. 494 U.S. at 209 (O'Connor, J., dissenting).

*Second*, while the Order recognizes that "*Bouligny* appeared to undercut *Russell*," it incorrectly reads *Carden* as "mak[ing] it clear that *Russell* still has precedential value and must be considered in any analysis of an association as a juridical person." *See* Order at 5. USAA believes that *Carden* does nothing of the sort. Instead, *Carden* completely adopts *Bouligny*'s reading of *Russell*, and expressly endorses *Bouligny*'s decision not to "apply [] *Russell* beyond its facts." 494 U.S. at 190 & n.2. Thus, *Bouligny* limited – and *Carden* eviscerated – the validity of *Russell* as a guide in determining the jurisdictional status of any entity other than the Puerto Rican sociedad en comandita. *See Id.* at 190.

*Third*, in all events, the Order fails to recognize that both the Supreme Court and the Ninth Circuit have limited *Russell*'s applicability to civil law entities. In other words, as the Supreme Court made clear in *Bouligny*, *Russell* addresses only the narrow problem of "fitting an exotic creation of the civil law . . . into a federal scheme which knew it not." 382 U.S. at 151. This civil law/common law distinction originates in *Russell* itself, where the Court drew a careful line between entities created under a civil law system, and entities organized within a common law structure. For example, the *Russell* Court emphasized the distinctive civil law system under which the sociedad en comandita was created, noting that while "[t]he tradition of the common law is to treat as legal persons only incorporated groups and to assimilate all others to partnerships . . . [, t]he tradition of the civil law, as expressed in the Code of Puerto Rico, is otherwise." 288 U.S. at 480. The distinction was confirmed in

*Bouligny*, 382 U.S. at 151, and strongly reiterated in *Carden*. In fact, the *Carden* court took pains to note that *Russell*, while not expressly overruled, had been limited to its facts. 494 U.S. at 190 & n.2. Finally, the Ninth Circuit has expressly relied on the civil law/common law distinction in analyzing *Russell*'s reach. In *Cohen v. Rosenfeld*, 733 F.2d 625, 628-29 (9th Cir.), *cert. denied*, 469 U.S. 932 (1984), the court noted the need to "distinguish[] 'the tradition of the common law' . . . from the more diverse tradition of the civil law as expressed in the Code of Puerto Rico," and then went on to apply *Russell* to the civil law entity at issue in that case (an anstalt organized under the laws of Liechtenstein, a civil law country). USAA thus believes that the Order plainly errs in applying *Russell* outside the civil law setting.[5]

B. In Light Of The Conceded Conflict Between The Order And The Decisions Of The Second And Tenth Circuits, There Plainly Is Substantial Ground For Difference Of Opinion

In addition to conflicting with *Carden*'s holding concerning the proper method for determining jurisdictional status, the Order concededly creates an express conflict with the Second and Tenth Circuits. As the Order itself notes (Order at 5), both *Baer v. USAA*, 503 F.2d 393 (2d Cir. 1974), and *Tuck v. USAA*, 859 F.2d 842 (10th Cir. 1988),

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[5] It should be noted in this regard that a reciprocal insurance exchange is hardly an "exotic" creature of Texas law. Many states authorize this type of entity, including California. *See* Calif. Ins. Code §§ 1280-1530 (West 1972 & Supp. 1992).

*cert. denied*, 489 U.S. 1080 (1989), have expressly considered USAA's jurisdictional status, and in both cases the courts held that USAA's citizenship must be determined by reference to all of its members. The courts have recognized that the existence of this type of conflict obviously means that there is "substantial grounds for difference of opinion." For example, the court in *SHR Limited Partnership v. Braun*, 888 F.2d at 456-57, granted § 1292(b) review in precisely this situation – there, as here, the court of appeals had yet to rule on the diversity jurisdiction issue that had led to "[a] split of authority." *See also Powell v. National Football League*, 711 F.Supp. 959, 961 (D.Minn.), *rev'd on other grounds*, 888 F.2d 559 (8th Cir. 1989) (citing conflicting decisions in finding that "[t]here is a substantial ground for difference of opinion"); *Kirchen v. Guaranty Nat'l Ins. Co.*, 422 F. Supp. 58, 61 (E.D. Wis. 1976) (noting existence of conflicting decisions would satisfy "substantial ground for difference of opinion" requirement).[6]

In sum, the Order plainly satisfies § 1292(b)'s second requirement. It simultaneously gives *Russell* a broad reading, thus creating a novel issue of law warranting § 1292(b) review, *see Klinghoffer v. S.N.C. Achille Lauro*, 921 F.2d 21, 25 (2d Cir. 1990), and creates a conflict with other decisions, thus evidencing the difference of opinion required for § 1292(b) review, *see SHR Limited Partnership v. Braun*, 888 F.2d at 456-57.

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[6] *Cf. Chalfin v. Beverly Enterprises, Inc.*, 745 F.Supp. 1117, 1122 (E.D. Pa. 1990) (noting, in denying request for § 1292(b) certification, that district court's decision agreed with only court of appeals decision on point).

III. Resolution Of The Jurisdictional Issue Through An Immediate Appeal Would Materially Advance The Ultimate Termination Of This Litigation

Section 1292(b)'s third requirement also is satisfied; resolution of the jurisdictional issue at this point would materially advance the ultimate termination of this litigation. As noted above, resolution of USAA's jurisdictional status controls whether this suit can proceed in federal court. USAA submits that there is a substantial likelihood that the Ninth Circuit will adhere to the reading of *Russell* it adopted in *Cohen v. Rosenfeld*, 733 F.2d at 628-30, and thus decline to accept the broader approach taken in the Order. In addition, USAA submits that the Ninth Circuit likely will follow the lead of the Second and Tenth Circuits, and that it therefore will reverse the Order's conclusion that USAA should be considered to be a corporation for diversity purposes. Thus, there is, at minimum, a substantial possibility that this case ultimately will be dismissed for lack of subject matter jurisdiction. Obtaining that ruling now from the Ninth Circuit obviously will "materially advance the ultimate termination of the litigation."

Moreover, it is important to recognize that the conflicting legal standards created by the Order place USAA in an untenable position. The Tenth Circuit has instructed USAA "to make . . . motions [to dismiss] in all pending diversity litigation." *Tuck v. USAA*, 859 F.2d at 845 n.3. The Order makes it impossible for USAA to follow this direction, and makes it difficult for USAA to know even how to characterize itself when faced with a diversity suit. Thus, USAA is compelled to seek to resolve this conflict, and the jurisdictional issue therefore eventually

must be addressed by the Ninth Circuit. Immediate appellate consideration of the issue will prevent substantial disorder and confusion, thereby preventing delay not only in this proceeding, but in all federal court proceedings in which USAA is named as a party. Certification therefore should be granted. *See* 16 C.Wright, A. Miller, E. Cooper & E. Gressman, *Federal Practice and Procedure* § 3930, at 163 & n.21.

Finally, the proceedings in this case are at their very outset. There has been no discovery, and the only legal arguments addressed by the parties have focused on the threshold jurisdictional issues. Thus, the parties must proceed with full discovery, brief and argue any legal issues, and prepare for a trial on the merits, and the Court must address the substantive issues in the case and preside over any trial. There are no special reasons for pressing on with these steps while the serious jurisdictional uncertainty remains unresolved,[7] and accordingly, there is a substantial potential savings involved in resolving the jurisdictional issue now, rather than after the parties and the court have been burdened with full discovery and a trial. These considerations indicate an interlocutory appeal will "materially advance" the progress of this litigation. *See* 16 C.Wright, A. Miller, E. Cooper & E. Gressman, *Federal Practice and Procedure* § 3930, at 163-68.

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[7] In fact, USAA has filed a separate motion for a stay of further proceedings in this case pending resolution of this motion to certify and the subsequent § 1292(b) appeal or if certification not granted, pending resolution of USAA's petition for a writ of mandamus.

In addition, the parties already have reviewed the jurisdictional issues in lengthy briefs to this Court, and the certified appeal thus could proceed with unusual dispatch. Specifically, to prevent any undue delay of the proceedings in this case, USAA will commit to filing its brief on the merits of the § 1292(b) appeal within the same 10-day period that the statute allows for the filing of the petition for leave to appeal from this Court's certification order. *See* 28 U.S.C. § 1292. USAA also will seek expedited briefing – and propose a 15-day period for Plaintiffs' brief and a 5-day period for USAA's reply brief – and expedited argument from the Ninth Circuit. In these circumstances allowing an immediate appeal of the jurisdictional issues resolved by the Order should cause no significant delay and should materially advance the termination of this suit.

## CONCLUSION

For the foregoing reasons, USAA's motion for certification pursuant to 28 U.S.C. § 1292(b) should be granted, and this Court should amend the February 7, 1992 Order to include the recitations called for by § 1292(b).

Respectfully submitted,

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Dated: February 11, 1992

**VERIFICATION**

STATE OF CALIFORNIA, COUNTY OF

I have read the foregoing _____

_____ and know its contents

[X] CHECK APPLICABLE PARAGRAPH

[ ] I am a party to this action. The matters stated in the foregoing document are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

[ ] I am [ ] an Officer [ ] a partner _____ [ ]

a _____ of _____

_____

a party to this action, and am authorized to make this verification for and on its behalf, and I make this verification for that reason. [ ] I am informed and believe and on that ground allege that the matters stated in the foregoing document are true. [ ] The matters stated in the foregoing document are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

[ ] I am one of the attorneys for _____ , a party to this action. Such party is absent from the county of aforesaid where such attorneys have their offices, and I make this verification for and on behalf of that party for that reason. I am informed and believe and on that ground allege that the matters stated in the foregoing document are true.

Executed on _____, 19 _____, at _____, California.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

_____ _____

Type or Print Name Signature

**PROOF OF SERVICE**
1013A (3) CCP Revised 5/1/88

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles , State of California.

I am over the age of 18 and not a party to the within action; my business address is: 555 West 5th Street, Suite 4600, Los Angeles, California 90013

On 2/11/ , 19 92 , I served the foregoing document described as Memorandum Of Points And Authorities In Support Of Defendant's Motion For Certification Pursuant To 28 U.S.C. Section 1292

on the interested parties in this action

[ ] by placing the true copies thereof enclosed in sealed envelopes addressed as stated on the attached mailing list:

[X] by placing [ ] the original [ ] a true copy thereof enclosed in sealed envelopes addressed as follows:

Frank M. Darras, Esq.
William M. Shernoff, Esq.
Shernoff, Bidart & Darras
600 South Indian Hill Blvd.
Claremont, CA 91711-5498

[X] BY MAIL

[ ] *I deposited such envelope in the mail at _____, California. The envelope was mailed with postage thereon fully prepaid.

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UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

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| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br>Plaintiffs,<br>v.<br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br>Defendant. | Case NO. CV-91-3615-WFN<br>MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT OF DEFENDANT'S MOTION FOR A STAY OF PROCEEDINGS PENDING REVIEW<br>(Filed Feb. 11, 1992)<br>(Judge Wm. Fremming Nielson)<br>Date: March 9, 1992<br>Time: 10:00 a.m.<br>Courtroom: To Be Announced<br>Trial Date: September 14, 1992 |

## INTRODUCTION

On February 7, 1992, this Court entered an Order denying defendant UNITED SERVICES AUTOMOBILE ASSOCIATION's ("USAA") motion to dismiss this case for lack of subject matter jurisdiction. USAA has filed, contemporaneously with this motion for a stay, a motion to certify the February 7, 1992 Order (the "Order") for immediate appeal pursuant to 28 U.S.C. § 1292(b) (1988). If that motion is not granted, USAA plans to file a petition for review in the form of a writ of mandamus.[1]

Since what is involved here is the threshold question of subject matter jurisdiction, further proceedings in this case should be stayed until such time as the Court of Appeals had considered jurisdictional issue. Such a stay will further the "just, speedy, and inexpensive determination of [this] action" (Fed. R. Civ. P. 1) by preventing the parties and Court from being subjected to the undue burden and expense of discovery and other proceedings in a case that may soon be determined to fall outside the Court's subject matter jurisdiction. In addition, because the Order places USAA in the untenable position of being unable even to characterize its correct jurisdictional status, USAA also requests a stay of the proceedings in this case should the Court not grant the motion to certify, in order to permit USAA to file, and the Court of Appeals to consider, a petition for mandamus.

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[1] USAA believes that, if the motion to certify is not granted, review may properly be had by way of a petition for mandamus. *See, e.g., Christensen v. United States District Court*, 844 F.2d 694, 696-97 (9th Cir. 1988).

## ARGUMENT

### Further Proceedings In This Case Should Be Stayed Until The Ninth Circuit Has Had An Opportunity To Review The Threshold Issue Of Subject Matter Jurisdiction

Section 1292(b) recognizes that a stay of proceedings pending resolution of a certified appeal may be appropriate. *See* 28 U.S.C. @ § 1292(b). Likewise, Rule 26(c) of the Federal Rules of Civil Procedure provides that all discovery may be stayed in order to avoid "undue burden or expense." Since the issue that USAA seeks to present through the certified appeal is a threshold question of subject matter jurisdiction, and since the short stay necessary here will cause Plaintiffs no substantial harm, this plainly is an appropriate case for such a stay.

*First*, the courts have regularly granted stays pending resolution of a § 1292(b) appeal. *See, e.g., Larraburu Bros., Inc. v. Royal Indem. Co.*, 604 F.2d 1208, 1210 (9th Cir. 1979); *Bigelow v. Hawaiian Airlines, Inc.*, 696 F. Supp. 1356, 1360 (D. Haw. 1987); *Rauch v. United Instruments, Inc.*, 405 F. Supp. 442, 447 (E.D. Pa. 1975), *rev'd on other grounds*, 548 F.2d 452 (3d Cir. 1976); *O'Brien v. Avco Corp.*, 309 F. Supp. 703, 705 (S.D.N.Y. 1969). Such a stay is particularly appropriate "when, as here, the determination of [the] preliminary question may dispose of the entire suit." *O'Brien v. Avco Corp.*, 309 F. Supp. at 705. The Order resolves the threshold question of whether this Court has subject matter jurisdiction over the action. But since it is well established that "the parties cannot by consent, waiver or estoppel obtain federal subject matter jurisdiction," *Sullivan v. First Affiliated Sec., Inc.*, 813 F.2d 1368, 1374 (9th Cir.), *cert. denied*, 484 U.S. 850 (1987), the Order does not

end the matter; the Ninth Circuit necessarily will consider the question and if it finds that jurisdiction is lacking it must order that the case be dismissed. Thus, by definition, determination of the jurisdictional issue "may dispose of the entire suit." *O'Brien v. Avco Corp.*, 309 F. Supp. at 705.

*Second*, a stay is particularly appropriate here because allowing discovery or other proceedings would lead to "undue burden or expense." Fed. R. Civ. P. 26(c). The future proceedings in this case will not involve the jurisdictional issue, but will center on the Plaintiffs' motion for sanctions and on the Plaintiffs' underlying allegations that USAA handled their insurance claim in bad faith. Should the Ninth Circuit ultimately reject this Court's conclusion that USAA should be treated as a corporation for diversity purposes, all of the parties' and the Court's efforts will be wasted, since the case then would be dismissed for lack of subject matter jurisdiction. USAA submits that there is a substantial likelihood of just such a result. USAA believes that the Order's analysis of, and conclusions about, USAA's jurisdictional status conflicts with the Supreme Court's decision in *Carden v. Arkoma Assocs.*, 494 U.S. 185 (1990), and with the Second and Tenth Circuit's decisions in *Baer v. USAA*, 503 F.2d 393 (2d Cir. 1974), and *Tuck v. USAA*, 859 F.2d 842 (10th Cir. 1988), *cert. denied*, 489 U.S 1080 (1989). Accordingly, there is a strong basis to believe that the Ninth Circuit will conclude that there is no subject matter jurisdiction and order that the case be dismissed. Allowing discovery and other proceedings to go forward in these circumstances would impose an undue burden and expense, and fly in the face of the federal courts' established policy to

defer or limit discovery until such a potentially dispositive preliminary issue has been resolved. *See, e.g., Scroggins v. Air Cargo, Inc.*, 534 F.2d 1124 (5th Cir. 1976); *Brennan v. Local Union No. 639, Int'l Brotherhood of Teamsters*, 494 F.2d 1092 (D.C. Cir. 1974); *Taylor v. Breed*, 58 F.R.D. 101 (N.D. Cal. 1973); *Kelleher v. Omark Indus., Inc.*, 19 Fed. R. Serv. 2d 725 (D. Mass. 1975). In short, a stay is necessary to serve the basic goal of "secur[ing] the just, speedy, and inexpensive determination of [this] action." Fed. R. Civ. P. 1.

*Third*, in the circumstances of this case, entry of a stay will not unduly harm the Plaintiffs. A stay "can in no way prejudice plaintiff[s] on the interlocutory appeal," *O'Brien v. Avco Corp.*, 309 F. Supp. at 705, since the issues to be addressed in the future proceedings in this case will in no way illuminate the jurisdictional issues presented by the Order. Nor will a stay impose any undue burdens on the Plaintiffs. The underlying issue in this litigation is whether USAA acted in bad faith in processing Plaintiffs' claim for losses caused by a fire in their home.[2] Recovery of damages for the alleged bad faith is the only issue in the case; there is no dispute concerning coverage. In fact, USAA already has agreed to pay for the reconstruction and repair of the damaged portions of the Plaintiffs' home, and that work is almost complete.

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[2] USAA will supply an affidavit to support the factual allegations in this paragraph. However, due to USAA's desire to file this motion as expeditiously as possible, it was not administratively feasible to submit an executed affidavit contemporaneously with this motion. The affidavit will be filed within the next several days.

*Finally,* granting a stay will not unduly delay these proceedings, since the appeal (or, if necessary, the petition for mandamus) can be undertaken in an expedited fashion. The legal issue involved in USAA's proposed certified appeal (or, if certification is denied, in USAA's planned mandamus action) already had been extensively briefed by the parties.[3] Briefing and argument in the Ninth Circuit therefore readily can be compressed to the point that a stay pending appeal will not indefinitely suspend the proceedings in this case. Specifically, immediately after this Court's ruling on the motion to certify, USAA will move for expedited briefing and consideration of the appeal by the Court of Appeals. USAA will propose that its brief on the merits of the § 1292(b) appeal be filed within the same 10-day period that the statute allows for filing the petition for leave to appeal from this Court's certification order, that Plaintiffs be given 15 days to file their brief, and that USAA be given 5 days to file its reply brief. Likewise, USAA commits to promptly filing any petition for mandamus should this Court not grant § 1292(b) certification, and to proposing a similar expedited schedule if the Ninth Circuit grant mandamus review. In sum, USAA will make every effort to move forward with appellate review of the jurisdictional issue as expeditiously as possible. Perhaps the best evidence of USAA's commitment in this regard is the fact that the motion for § 1292(b) certification and this motion for a

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[3] For this reason, USAA is planning to file an ex parte application for an order shortening the time for consideration of this motion and the motion to certify.

stay are filed on the first business day following this Court's entry of the Order.

## CONCLUSION

For the foregoing reasons, USAA motion for a stay of proceedings pending review should be granted, and this Court should enter an order staying discovery and all other proceedings in this case until the later of: (i) resolution of USAA's pending motion for certification pursuant to 28 U.S.C. § 1292(b) and of the resulting certified appeal; and (ii) resolution of USAA's petition for mandamus, which will be filed if the motion for certification is not granted.

Respectfully submitted,

DANIELS, BARATTA & FINE

By: /s/ Paul R. Fine
Paul R. Fine

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE ASSOCIATION

Of Counsel:

JONES, DAY, REAVIS & POGUE
1450 G Street, N.W.
Washington, D.C. 20005
(202) 879-3939

Dated: February 11, 1992

## VERIFICATION

STATE OF CALIFORNIA, COUNTY OF

I have read the foregoing _____

_____ and know its contents

[X] CHECK APPLICABLE PARAGRAPH

[ ] I am a party to this action. The matters stated in the foregoing document are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

[ ] I am [ ] an Officer [ ] a partner _____ [ ]

a _____ of _____

_____

a party to this action, and am authorized to make this verification for and on its behalf, and I make this verification for that reason. [ ] I am informed and believe and on that ground allege that the matters stated in the foregoing document are true. [ ] The matters stated in the foregoing document are true of my own knowledge except as to those matters which are stated on information and belief, and as to those matters I believe them to be true.

[ ] I am one of the attorneys for _____ , a party to this action. Such party is absent from the county of aforesaid where such attorneys have their offices, and I make this verification for and on behalf of that party for that reason. I am informed and believe and on that ground allege that the matters stated in the foregoing document are true.

Executed on _____, 19 _____, at _____, California.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Type or Print Name _____ Signature _____

**PROOF OF SERVICE**
1013A (3) CCP Revised 5/1/88

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California.

I am over the age of 18 and not a party to the within action; my business address is: 555 West 5th Street, Suite 4600, Los Angeles, California 90013

On 2/11/, 19 92. I served the foregoing document described as Memorandum Of Points And Authorities In Support Of Defendant's Motion For A Stay Of Proceedings Pending Review

_____ on the interested parties in this action

[ ] by placing the true copies thereof enclosed in sealed envelopes addressed as stated on the attached mailing list:

[X] by placing [ ] the original [x] a true copy thereof enclosed in sealed envelopes addressed as follows:

Frank M. Darras, Esq.
William M. Shernoff, Esq.
Shernoff, Bidart & Darras
600 South Indian Hill Blvd.
Claremont, CA 91711-5498

[X] BY MAIL

[ ] *I deposited such envelope in the mail at

_____, California.

The envelope was mailed with postage thereon fully prepaid.

[X] As follows: I am "readily familiar" with the firm's practice of collection and processing correspondence for mailing.

Under that practice it would be deposited with U.S. postal service on that same day with postage thereon fully prepaid at Los Angeles California in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after date of deposit for mailing in affidavit.

Executed on February 11, , 19 92 , at

Los Angeles , California.

[ ] **(BY PERSONAL SERVICE) I delivered such envelope by hand to the offices of the addressee.

Executed on _____, 19 _____, at

_____, California.

[ ] (State) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Martha Espelage — Type or Print Name

/s/ Martha Espelage — Signature

WILLIAM M. SHERNOFF, #38856
MICHAEL J. BIDART, #60852
FRANK N. DARRAS, #128904
GARY L. TYSCH, #128389
Members of the Firm
SHERNOFF, BIDART & DARRAS
600 South Indian Hill Boulevard
Claremont, California 91711-5498
(714) 621-4935

Attorneys for Plaintiff

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. 91 3615 JSL (GHKx)<br><br>OPPOSITION TO MOTION FOR CERTIFICATION AND MOTION TO STAY PROCEEDINGS; MEMORANDUM OF POINTS AND AUTHORITIES<br><br>Date: February 28, 1992<br>Time: 8:45 a.m.<br>Room: Telephonic Argument |

TO ALL PARTIES AND TO THEIR ATTORNEYS OF RECORD:

Plaintiffs LAUGHLIN E. WATERS and VOULA D. WATERS hereby oppose the Motion for Certification and the Motion to Stay Proceedings of defendant UNITED SERVICES AUTOMOBILE ASSOCIATION ("USAA") on the grounds that the issues presented are not appropriate for interlocutory review, on the grounds that the motions presented are nothing more than further evidence of USAA's penchant for forum-shopping and on the further grounds that stay of the proceedings is not warranted or justified.

Plaintiffs' opposition is based on this Opposition, the attached Memorandum of Points and Authorities, all papers, pleadings and records on file in this action and on such other and further argument and evidence as may be presented.

Dated this 25 day of February, 1992 at Claremont, California.

SHERNOFF, BIDART & DARRAS

By: /s/ W M S
William M. Shernoff
Attorneys for Plaintiff

## MEMORANDUM OF POINTS AND AUTHORITIES

### 1.

### INTRODUCTION

Plaintiffs and their counsel are dismayed at USAA's current conduct in seeking to obtain interlocutory review of the order denying the motion to dismiss and in seeking a further stay of this action. USAA was content to waste

the time, money, resources and judicial talent of the litigants and courts in the 172 cases documented in plaintiffs' motion for sanctions. In those cases, USAA laid in wait. If the results were favorable, USAA would remain silent about the jurisdictional issues. If the results were bad, USAA would put out all the stops to challenge jurisdiction so it could engage in its decade-long game of jurisdictional hopscotch. In light of USAA's past conduct, the present motions are a slap in the face to the Ninth Circuit.

USAA has presented no plausible reason for further delaying this action by requiring a stay of the proceedings and permitting interlocutory review. Moreover, USAA's veiled threat that if the motion for interlocutory review is not granted, it will seek a writ of mandamus is yet another "power play" tactic which exemplifies USAA's "win at any cost" attitude. It is just this attitude which justifies an award of sanctions in this case.

2.

THERE IS NO JUSTIFICATION FOR STAYING THE DETERMINATION OF THE SANCTIONS ISSUE

In conjunction with its motion for interlocutory appeal, USAA seeks to stay the pending discovery and pending hearing on plaintiffs' motion for sanctions. Such a stay is unjustified and unwarranted.

First, the stay should not be granted for the simple reason that USAA has failed to present a plausible basis for interlocutory appeal. USAA's request is premised on the assumption that this Court will certify the matter for interlocutory appeal, that the Ninth Circuit will accept

the appeal and that USAA will prevail. Those represent USAA's "wish list", but do not reflect reality. As noted in *Robbins Co. v. Lawrence Manufacturing Co.*, 482 F.2d 426 (9th Cir. 1973), interlocutory appeal will be granted only extraordinary cases. Aside from USAA's tortious destruction of Federal decorum and unrivaled tampering with the administration of justice, this is not an extraordinary case. USAA's failed attempt to stay this action and obtain appeal is another calculated, cunning affort to waste the judicial time and resources of this Court and the other parties and delay this action. Since USAA's chance of obtaining interlocutory appeal are remote, at best, there is no justifiable basis for staying or delaying this case any further.

Second, even if interlocutory appeal were granted, even if the Ninth Circuit agreed to accept the appeal and even assuming the Ninth Circuit ultimately determined there was no jurisdiction, that would not affect the sanction issue. As noted in plaintiff's motion for sanctions, and which has never been disputed by USAA, this Court has the power to sanction USAA's conduct even if it were ultimately determined that this Court has no jurisdiction. (*Cooter & Gell v. Hartmarx Corp.*, ___ U.S. ___, 110 S.Ct. 2447, 2455, 110 L.Ed.2d 359 (1990); *Eash v. Riggins Trucking, Inc.*, 757 F.2d 557 (3rd Cir. 1985).) There is thus no justification whatsoever for further delaying the determination of the sanctions issue in this case.

Indeed, the fact that the sanction issue remains pending serves as yet another basis for denying interlocutory review. No doubt, USAA will seek to obstruct, delay and challenge any imposition of sanctions by this honorable Court. Permitting USAA interlocutory appeal now will

only cause further duplicative effort when USAA challenges the sanction award.

USAA should not be permitted to allow is [sic] tactical antics to further delay determination of plaintiffs' sanction request. Since interlocutory appeal is not appropriate in this case and since there is no further justifiable basis for ordering a stay of the discovery regarding sanctions or the sanction hearing itself, the stay should be denied.

3.

STAY OF DISCOVERY IN THIS ACTION IS COMPLETELY UNWARRANTED AND UNJUSTIFIED

First USAA refused to provide responses to plaintiffs' discovery requests in this action on the basis that jurisdiction was in issue. Now that this Court has determined that there is jurisdiction of this matter, USAA seeks to further delay plaintiffs' discovery. Such a request is outrageous, unjustifiable and itself a basis for sanctions.

4.

THERE IS NO SUFFICIENT BASIS TO JUSTIFY INTERLOCUTORY APPEAL ON THE ISSUE OF JURISDICTION IN THIS CASE

The jurisdictional issue which USAA wishes to have reviewed by the Ninth Circuit was superbly briefed and ably argued and this Court's order was well-reasoned. Interlocutory review may be obtained only where the order under review involves:

a. A question of law;

b. Which is controlling;

c. On which there is substantial ground for difference of opinion; and

d. In which an immediate appeal will materially advance the ultimate termination of the litigation. (28 U.S.C. section 1292(b).)

Absent every one of those factors, interlocutory review cannot be granted. All be [sic] factors necessary to permit interlocutory review are simply not present.

(1) The matter is not simply "a question of law".

As noted in plaintiffs' opposition to the Motion to Dismiss, the issue of jurisdiction has an inherent factual underpinning. (*Thornhill Publishing Co., Inc. v. General Telephone & Electronics Corp.*, 594 F.2d 730 (9th Cir. 1979).) Since there are issues of fact concerning USAA's status as a corporation *under Texas law* which relate to and are determinative of the jurisdictional issue, interlocutory appeal is not warranted.

(2) The issue presented is not "controlling" on the merits of this action.

Although USAA argues that the jurisdictional issue will make this case go away, USAA is being very shortsighted. The merits of this action relate to USAA's bad faith and the determination of the jurisdictional issue will have no effect on that whatsoever. If this action were tried to a jury and the jury finds in favor of plaintiffs, even if the Ninth Circuit later determined there was no

jurisdiction, the likelihood that USAA would retry the entire action rather than settling is virtually nonexistent. Thus, even if the jurisdictional issue is later decided in USAA's favor, the trial will have served its purpose and the matter would be resolved without any waste of judicial and litigant resources. Similarly, if plaintiffs lose on the jurisdictional issue, the same trial will still be necessary. An adverse ruling on the jurisdictional issue simply will not resolve the *merits* of the action.

(3) There is no substantial ground for difference of opinion.

Despite the fact that USAA has presented decisions from two other circuits, there is no proper basis for finding that those decisions create a substantial ground for differences of opinion. USAA has failed to show that those other courts considered, in ruling on the jurisdictional issue, and the effect of the changes in Texas corporation law which expressly defines a reciprocal insurance exchange as a corporation. Absent that showing, the other decisions are meaningless.

It is ironic that USAA suddenly claims that its federal diversity jurisdiction status is now a basis for difference of opinion in light of its decade of effort in invoking federal jurisdiction when it suited USAA's purpose.

Finally, the fact that other circuits have ruled in one way on a matter is not controlling on either this court or the appellate courts of this circuit. Indeed, the Ninth Circuit has expressly ruled that the decisions of the Second Circuit (*California State Bd. of Equalization of Goggin*, 245 F.2d 44 (9th Cir. 1957), *cert. den.*, 353 U.S. 961, 77 S.Ct.

863, 1 L.Ed.2d 910) and the Tenth Circuit (*Strand v. Schmittroth*, 251 F.2d 590 (9th Cir. 1958), *cert. dis.*, 355 U.S. 896, 78 S.Ct. 258, 2 L.Ed.2d 186) are not binding on it.

(4) Appeal now will not materially advance the ultimate termination of the litigation.

Since the same bad faith issues will have to be litigated, no matter what the forum, appeal now will not significantly advance the *ultimate* termination of this litigation. This is a simple, straightforward bad faith case. USAA has no valid defense to its bad faith actions. There are no issues of policy interpretation. There are no issues of complex valuation. In fact, in short order, the only remaining issues will be USAA's liability for its bad faith conduct. This is a case where USAA "low-balled" the wrong folks and the evidence of that is simple and straightforward. In fact, plaintiffs could try this case in less than a week and are willing to have the trial date advanced to a week following the hearing on the sanctions issue. Thus, the entire matter can be resolved expeditiously and the entire matter appealed after final judgment.

5.

EVEN IF USAA HAD ESTABLISHED A PROPER BASIS FOR INTERLOCUTORY REVIEW, THIS CASE SIMPLY DOES NOT WARRANT IT

Even if USAA had established that the factors necessary for interlocutory review were present, certification is not warranted in this case. Interlocutory review is granted "only in extraordinary circumstances where the

decision might avoid protracted and expensive litigation." (*Robbins, supra.*) Interlocutory review is *not* to be granted in ordinary actions that can be tried on their merits in a few days. (*Cardwell v. Chesapeake & Ohio Railway*, 504 F.2d 444 (6th Cir. 1974).) As noted, this action *can* be tried in a few days. *All* the issues can be resolved and one appeal taken from the final judgment. Denying interlocutory review now will not foreclose USAA's right to challenge jurisdiction after final judgment. Nothing will be lost and, should USAA come to its senses in the meantime and settle this action, much will be gained by preventing the waste of judicial resources in this Court, in the Ninth Circuit Court and in the Supreme Court by precluding USAA's ability to further delay this action now.

6.

## CONCLUSION

USAA has failed to provide any justifiable basis for invoking the extraordinary remedy of interim review. USAA has presented no new factual or legal arguments which justifies this Court impeding the timely progress of this action. Indeed, USAA's motions are nothing more than further evidence of its hardball tactics which will burden this court, the appellate court and the litigants without dealing with the merits of a case. Having failed to do so, USAA's motions should be denied.

Dated this 25 day of February, 1992 at Claremont, California.

SHERNOFF, BIDART & DARRAS

By: /s/ W M Shernoff
William M. Shernoff
Attorneys for Plaintiff

## PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On FEB. 25 1992, I served the foregoing document described as:

OPPOSITION TO MOTION FOR CERTIFICATION AND MOTION TO STAY PROCEEDINGS; MEMORANDUM OF POINTS AND AUTHORITIES

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as follows:

Paul R. Fine, Esq.
Daniels, Baratta & Fine
1801 Century Park East
Ninth Floor
Los Angeles, California
90067
(213) 556-7900
FAX: (213) 556-2807

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE
ASSOCIATION

COURTESY COPY TO: JUDGE WM. FREMMING NIELSEN

---

[X] BY MAIL

I caused such envelope to be deposited in the mail at Claremont, California. The envelope was mailed with postage thereon fully prepaid. I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal service on that same day in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date deposit for mailing in affidavit.

[ ] BY PERSONAL SERVICE

I caused to be delivered by hand to the above-listed addressees or to the addressees on the list attached hereto.

[ ] BY OVERNIGHT MAIL/COURIER

To expedite the delivery of the above-named document, said document was sent via overnight courier for next day delivery to:

[X] BY FACSIMILE ("FAX")

In addition to the manner of proof of service indicated above, a copy was sent by FAX to:

Paul Fine, Esq. / Daniels, Baratta & Fine / (213) 556-2807

February 25, 1992 at approx. 4:15 PM.

[ ] (State) I declare under penalty of perjury under the laws of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Executed on FEB. 25 1992, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

UNITED STATES DISTRICT COURT
CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS and VOULA D. WATERS, Plaintiffs, -vs- UNITED SERVICES AUTOMOBILE ASSOCIATION, Defendant. | NO. CV-91-3615-WFN<br><br>ORDER DENYING MOTIONS FOR CERTIFICATION AND TO STAY PROCEEDINGS<br><br>(Filed Mar 16, 1992) |

THIS CONSTITUTES NOTICE OF ENTRY
AS REQUIRED BY FRCP, RULE 77(d)

Before the Court are defendant's Motions to Certify a Court Order for Appeal and for stay Pending Appeal, heard on February 28, 1992 before the Honorable Wm. Fremming Nielsen. Appearing telephonically were William Shernoff and Frank Darras for plaintiffs; and Paul Fine and Timothy Dyk for defendant. Having reviewed the record, having heard the oral argument of counsel and being fully advised, this Court **DENIES** the motions for certification and stay.

Plaintiffs initiated this diversity action against their insurer, United Services Automobile Association [USAA], seeking amounts allegedly due under their insurance contract and alleging bad faith on the part of USAA in denying these sums. USAA moved for dismissal based on lack of subject matter jurisdiction, alleging that USAA is a non-corporate entity with members who reside in the state of California and therefore a non-diverse party. By

Order entered February 7, 1992, this Court held that USAA could be treated like a corporation for diversity purposes and therefore this Court has subject matter jurisdiction in this instance. It is this Order that USAA wishes to appeal and proposes a stay of proceedings pending that review.

Without question "there is a strong policy behind the rule that appeals are to be made only following final judgment on the merits." *In re Cement Antitrust Litigation* (MDL No. 296), 673 F.2d 1020, 1023 (9th Cir. 1982). However, there are exceptions to that rule, one of which is found at 28 U.S.C. § 1292(b) (1988) which provides in pertinent part:

> When a district judge . . . shall be of the opinion that [an] order involves a controlling question of law as to which there is substantial ground for difference of opinion and that an immediate appeal from the order may materially advance the ultimate termination of the litigation, he shall so state in writing in such order. . . . [A]pplication for an appeal hereunder shall not stay proceedings in the district court unless the district judge or the Court of Appeals or a judge thereof shall so order.

From this rule case law has singled out three components necessary for certification, they are "(1) that there be a controlling question of law, (2) that there be substantial grounds for difference of opinion, and (3) that an immediate appeal may materially advance the ultimate termination of the litigation." *Cement Antitrust Litigation*, 673 F.2d at 1026. Unquestionably the first two elements are met in this case; i.e., whether this Court has subject matter jurisdiction is a controlling question of law and

the fact that the Second and Tenth Circuits have held that USAA citizenship must be determined by reference to all of its members indicates that there are substantial grounds for difference of opinion. However there are serious questions whether an appeal will materially advance the ultimate termination of this litigation.

This is not the type of appeal that will terminate the dispute altogether as could a statute of limitations determination. Though reversal of this Court's Order by the Court of Appeals would terminate jurisdiction as to the merits of this case, still pending would be the important issue of whether sanctions should be levied against USAA for their conduct in federal court. *See Cooter & Gell v. Hartmarx Corp.*, 496 U.S. 384 (1990) ("[C]ourt may consider collateral issues after an action is no longer pending."). This Court has set a hearing on the sanctions issue for May 14, 1992, therefore if this Court were to grant certification for appeal of the February 7, 1992 Order, it would be promoting the piecemeal litigation so abhorred by the general rule which only permits appeal from a final order.

The Ninth Circuit has adopted a narrow approach to interlocutory appeals, "[t]he precedent in this circuit has recognized the congressional directive that Section 1292(b) is to be applied sparingly and only in exceptional cases." *Cement Antitrust*, 673 F.2d at 1027. *Cement Antitrust* defined exceptional situations as those "in which allowing an interlocutory appeal would avoid protracted and expensive litigation." *Id.* at 1026. This is not protracted litigation. Since USAA indicates a need to immediately resolve the conflict between the circuits as to jurisdiction, the Waters have indicated that they would be

willing to have the case moved from its current September trial date to June in order to expedite a final decision from which USAA could appeal. This is in no way protracted as the Court has now reset the trial to June 22, 1992. As the appeal should rightfully wait at least until the sanctions issue is determined, the delay of a mere six weeks for a final determination does not, in this Court's opinion, represent an unjust burden when, if the Court's prior Order is affirmed, the entire litigation may come to an end. This is not a complex case, it can be dealt with efficiently and quickly and clearly is not the type that was within the contemplation of Congress when they wrote the exception to the rule of final appeals in 28 U.S.C. § 1292(b). *See* also *Cardwell v. Chesapeake & Ohio Ry. Co.*, 504 F.2d 444, 446-47 (6th Cir. 1974) ("ordinary suit for personal injuries or wrongful death that can be tried and disposed of on its merits within a few days . . . should not be considered on interlocutory appeal").

Finally, USAA contends that a stay of the proceedings is necessary to avoid undue burden or expense. This argument is devoid of merit. This case will proceed whether in state or federal court, and the same substantive rules of law will be applied. USAA has advanced no argument on how following the Federal Rules of Civil Procedure will unduly prejudice them as opposed to following a state rule of procedure. Further, it is axiomatic that discovery is best completed as soon as possible after the incident at issue.

The parties are also in disagreement regarding the Waters' request for documents from USAA served in the form of a subpoena. The Waters assert that this form was chosen in order to make sure the materials were available

in time to review them for the sanctions hearing in May. USAA asserts that a subpoena is inappropriate and the material should be requested through the discovery process. The parties have agreed to a March 16, 1992 deadline for the documents to be produced, and that any objections on the part of USAA will be well in advance to have this matter resolved before the hearing. Accordingly,

**IT IS ORDERED** that:

1. The motion for Certification for Appeal and the Motion for Stay Pending Review are hereby **DENIED.**

2. The trial date of September 14, 1992 is **moved up to June 22, 1992 at 9:00 a.m.** The Clerk will notify the parties as to the courtroom assignment prior to trial.

3. The sanctions hearing shall be **continued from May 11, 1992 to May 14, 1992 at 1:30 p.m.** The clerk will notify the parties as to the courtroom assignment prior to the hearing.

4. USAA shall treat the Waters' subpoena as a request for documents and **respond by March 16, 1992.** If USAA plans to object to his request, it shall do so well in advance of the March 16, 1992 date and this Court will expedite any hearing regarding such objections.

**IT IS SO ORDERED.** The Clerk is hereby **DIRECTED** to enter this Order and forward copies to counsel.

**DATED** this 11 day of March, 1992.

/s/ Wm. Fremming Nielsen
WM. FREMMING NIELSEN
UNITED STATES DISTRICT JUDGE

WILLIAM M. SHERNOFF, #38856
MICHAEL J. BIDART, #60852
FRANK N. DARRAS, #128904
GARY L.TYSCH, #128389
D. SCOTT MOHNEY, #124426
Members of the Firm
SHERNOFF, BIDART & DARRAS
600 South Indian Hill Boulevard
Claremont, California 91711-5498
(714) 621-4935

Attorneys for Plaintiffs

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS and VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. CV-91-3615-WFN<br><br>FORMAL REQUEST FOR DISCOVERY AND PRODUCTION OF DOCUMENTS AND THINGS FOR INSPECTION, COPYING OR PHOTOGRAPHING PURSUANT TO FEDERAL RULES OF CIVIL PROCEDURE, RULE 34 |

DEMANDING PARTY: Plaintiffs, LAUGHLIN E. WATERS and VOULA D. WATERS

RESPONDING PARTY: Defendant, UNITED SERVICES AUTOMOBILE ASSOCIATION

SET NO.: ONE

TO THE DEFENDANT, UNITED SERVICES AUTOMOBILE ASSOCIATION, AND TO ITS ATTORNEYS OF RECORD:

Pursuant to the Federal Rules of Civil Procedure, Rule 34, plaintiffs hereby formally demand production and inspection of the following documents at the hour of 10:00 a.m. on MAR. 18, 1992, at the office of plaintiffs' attorneys located at 600 South Indian Hill Boulevard, Claremont, California.

The manner of inspection shall be personal inspection including the copying or photographing by or on behalf of the plaintiffs the below-mentioned documents, and other tangible things. If you withhold any documents requested because you claim a privilege, state the privilege claimed for each and every document, describe each document by its author, describe the name and occupation of the author, describe the name and occupation of each recipient, date of issuance, who, if anyone, received a copy of the document, and its general subject mater, including a brief description of the nature and context. Please number the documents produced sequentially to conform with the order in which the documents are maintained in your files.

A personal appearance by defendant and/or counsel is not required if defendant will submit copies of the documents described below with their verification, executed under penalty of perjury, verifying that the copies provided are accurate and true copies of the complete records requested.

PLEASE NOTE: Federal Rules of Civil Procedure, rule 34(b) requires two acts for compliance with this request:

(1) Service of a written response under oath within 30 days; and

(2) Production of documents or tangible things on or before the date of production specified above.

DEFINITION

(1) The term "writings" refers to all writings as defined in Federal Rules of Evidence, rule 1001.

The following designated items for discovery and production pertain to Homeowners Policy number 165 45 98 92A ("the Policy") and the claim which was filed by plaintiffs pursuant to said Policy, and which is the subject of this litigation.

1. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: Homeowners Policy number 165 45 98 92A issued by defendant to plaintiffs on or about July 15, 1990 including all attachments, endorsements, amendments, and/or riders from date of first issue to plaintiffs until the present;

2. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: The complete claim file (whether home office, regional office, local or other office) pertaining to the claim listed above from December 17, 1990 to the present including, but not limited to, the file folder or file;

3. All inter-office memoranda or other form of written communication of any employee of defendant relating to the initial processing of the claim listed above when defendant first received said claim;

4. All inter-office memoranda or other form of written communication from any employee of defendant relating to the continued processing of plaintiffs' claim listed above;

5. All written communication between plaintiffs and defendant, including all proof of loss forms;

6. All written communication between defendant and any third party concerning the processing, acceptance, or denial of the claim listed above;

7. All medical and investigative reports concerning plaintiffs and the claim listed above, and all written communication between defendant and any third party concerning said report or reports;

8. All inter-office memoranda or other form of written communication from any employee of defendant concerning denial of the claim listed above;

9. All written communication between defendant and plaintiffs concerning denial of the claim listed above;

10. all written communication between defendant and any third party or third party's attorney concerning denial of the claim listed above;

11. All photographs, motion pictures, videotapes or investigative reports of defendant concerning plaintiffs taken by or on behalf of defendant, relating to the processing or denial of the claim listed above;

12. All other written documents including correspondence, telephone notes, Telex, and fax pertaining to the processing of the above claim in the possession of defendant not designated in requests numbers 1 through 11;

13. All file folders or file jackets and adjacent or related exhibit folders in which any documents or other materials or items described in requests numbered 1 through 12 above are filed or maintained;

14. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: The complete and original underwriting file pertaining to the above-mentioned Policy from January 1, 1990 to the present including, but not limited to, the file folder or file folders themselves, adjacent exhibit folders, all papers, documents, and investigative reports directly pertaining to the above-mentioned Policy including but not limited to inter-office memoranda or notes pertaining to the issuance of the above-mentioned Policy, and any and all written communications or statements made between defendant and other parties, which directly pertain to issuance of the above-mentioned Policy to plaintiffs;

15. Any and all documents designated in requests numbered 1 through 14 that are located outside of or apart from the claim or underwriting file;

16. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: The complete claims manuals and/or procedures manuals, policy statements or memoranda which set forth company practices or policies

regarding the handling, processing and/or investigation of claims submitted by your insured and which was or should have been utilized by you at the time plaintiffs' claim, submitted pursuant to the above-referenced Policy, was handled, processed and/or investigated;

17. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: All additions, revisions, deletions or other changes that have been made in the above-referenced claims manuals and/or procedures manuals from the time plaintiffs' claim was submitted up to and including the present;

18. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: Any other documents including, but not limited to, inter-office memoranda, notes, files or reports outlining or describing procedures for claims handling, processing and investigation and which were or should have been utilized by you at the time plaintiffs' claim was handled, processed and/or investigated;

19. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: Any and all "writings" which constitute all advertising, sales, promotional and/or marketing materials, including sales, promotional, marketing and/or advertising brochures, pamphlets, memoranda and/or letters, or any other type of "writings" whatsoever, used by your company to sell, promote, market and/or advertise the type of insurance coverage which is the subject matter of this action to the

general public, including, but not limited to, multiple employer trusts, employer groups and/or individuals for the time period January 1, 1990 to July 1, 1990;

20. Pursuant to 28 U.S.C. section 1732, a true and correct copy of the following item which has been kept in the regular course of business: Any and all "writings" which constitute all advertising, sales, promotional and/or marketing materials, including sales, promotional, marketing and/or advertising brochures, pamphlets, memoranda and/or letters, or any other type of "writings" whatsoever, provided by your company to your sales force of agents and/or employees to guide, explain, instruct or teach them your company's preferred and/or designed method of promoting, marketing, advertising and/or selling the type of insurance coverage which is the subject matter of this action to the general public, including, but not limited to, multiple employer trusts, employer groups or individuals for the time period January 1, 1990 to July 1, 1990.

DATED This 14 day of February, 1992, at Claremont, California.

SHERNOFF, BIDART
& DARRAS

By: /s/ Frank N. Darras
FRANK N. DARRAS
Attorneys for Plaintiffs

## PROOF OF SERVICE

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On FEB. 14 1992, I served the foregoing document described as:

FIRST SET OF REQUEST FOR PRODUCTION OF DOCUMENTS PROPOUNDED TO USAA

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [X] a true copy thereof enclosed in sealed envelopes addressed as follows:

Paul R. Fine, Esq.
Daniels, Baratta & Fine
1801 Century Park East
Ninth Floor
Los Angeles, California
90067
(213) 556-7900
FAX: (213) 556-2807

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE
ASSOCIATION

---

[X] BY MAIL

I caused such envelope to be deposited in the mail at Claremont, California. The envelope was

mailed with postage thereon fully prepaid. I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal service on that same day in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date deposit for mailing in affidavit.

[ ] BY PERSONAL SERVICE

I caused to be delivered by hand to the above-listed addressees or to the addressees on the list attached hereto.

[ ] BY OVERNIGHT MAIL/COURIER

To expedite the delivery of the above-named document, said document was sent via overnight courier for next day delivery to:

[ ] BY FACSIMILE ("FAX")

In addition to the manner of proof of service indicated above, a copy was sent by FAX to:

[ ] (State) I declare under penalty of perjury under the laws of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Executed on FEB. 14 1992, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

WILLIAM M. SHERNOFF, #38856
MICHAEL J. BIDART, #60852
FRANK N. DARRAS, #128904
GARY L. TYSCH, #128389
D. SCOTT MOHNEY, #124426
Members of the Firm
SHERNOFF, BIDART & DARRAS
600 South Indian Hill Boulevard
Claremont, California 91711-5498
(714) 621-4935

Attorneys for Plaintiffs

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No.<br>CV-91-3615-WFN<br><br>INTERROGATORIES |

PROPOUNDING PARTY: Plaintiffs, LAUGHLIN E. WATERS and VOULA D. WATERS

RESPONDING PARTY: Defendant, UNITED STATES [sic] SERVICES AUTOMOBILE ASSOCIATION

SET NO.: ONE

TO THE DEFENDANT, UNITED STATES [sic] SERVICES AUTOMOBILE ASSOCIATION, AND TO ITS ATTORNEYS OF RECORD:

Plaintiffs request that pursuant to Federal Rules of Civil Procedure, rule 33, each of the following interrogatories be answered fully, separately, and under oath within thirty (30) days by defendant.

INTERROGATORIES

1. List the names and addresses of all individuals acting on your behalf, other than individuals performing merely clerical functions, who were involved in the handling of plaintiffs' claim which is the subject matter of this litigation.

2. For each of the individuals named in response to interrogatory no. 1 above, please state the job title or classification held by that individual at the time that individual handled the claim.

3. For each of the individuals named in response to interrogatory no. 1 above, please state the current title or job classification held by that individual.

4. For any individual named in response to interrogatory no. 1 above who no longer works for your company, please provide his or her last known address.

5. Of those persons listed in response to interrogatory no.1 above, please state the names of those individuals in a MANAGERIAL CAPACITY [the term MANAGERIAL CAPACITY is defined as whether that employee could dispose of the insurance claim with little or no supervision; it is the degree of discretion the

employee possesses in making a decision and not his/her "level" in the corporate hierarchy] who made the decision to offer the proposal that was communicated to plaintiffs in the May 30, 1991 letter.

6. Is defendant, UNITED SERVICES AUTOMOBILE ASOCIATION, relying on the advice of counsel as a defense in this case?

Dated this 14 day of February, 1992 at Claremont, California.

SHERNOFF, BIDART
& DARRAS

By: /s/ Frank N. Darras
FRANK N. DARRAS
Attorneys for Plaintiffs

**PROOF OF SERVICE**

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On FEB. 14 1992, I served the foregoing document described as:

FIRST SET OF INTERROGATORIES PROPOUNDED TO USAA

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [X] a true copy

thereof enclosed in sealed envelopes addressed as follows:

Paul R. Fine, Esq.
Daniels, Baratta & Fine
1801 Century Park East
Ninth Floor
Los Angeles, California
90067
(213) 556-7900
FAX: (213) 556-2807

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE
ASSOCIATION

---

[X] BY MAIL

I caused such envelope to be deposited in the mail at Claremont, California. The envelope was mailed with postage thereon fully prepaid. I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal service on that same day in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation date or postage meter date is more than 1 day after date deposit for mailing in [sic] affidavit.

[ ] BY PERSONAL SERVICE

I caused to be delivered by hand to the above-listed addressees or to the addressees on the list attached hereto.

[ ] BY OVERNIGHT MAIL/COURIER

To expedite the delivery of the above-named document, said document was sent via overnight courier for next day delivery to:

[ ] BY FACSIMILE ("FAX")

In addition to the manner of proof of service indicated above, a copy was sent by FAX to:

[ ] (State) I declare under penalty of perjury under the laws of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at those [sic] direction the service was made.

Executed on FEB. 14 1992, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

WILLIAM M. SHERNOFF, #38856
MICHAEL J. BIDART, #60852
FRANK N. DARRAS, #128904
GARY L. TYSCH, #128389
D. SCOTT MOHNEY, #124426
Members of the Firm
SHERNOFF, BIDART & DARRAS
600 South Indian Hill Boulevard
Claremont, California 91711-5498
(714) 621-4935

Attorneys for Plaintiff

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS,<br><br>Plaintiffs,<br><br>v.<br><br>UNITED SERVICES AUTOMOBILE ASSOCIATION,<br><br>Defendant. | Case No. CV-91-3615-WFN<br><br>INTERROGATORIES |

PROPOUNDING PARTY: PLAINTIFFS, LAUGHLIN E. WATERS AND VOULA D. WATERS

RESPONDING PARTY: DEFENDANT, UNITED SERVICES AUTOMOBILE ASSOCIATION

SET NO.: Two

TO THE DEFENDANT, UNITED SERVICES AUTOMOBILE ASSOCIATION, AND TO ITS ATTORNEYS OF RECORD:

Plaintiff requests that pursuant to Federal Rules of Civil Procedure, rule 33, each of the following interrogatories be answered fully, separately, and under oath within thirty (30) days by defendant.

## INSTRUCTIONS

In answering these interrogatories, you are required to furnish information not only within your own knowledge or obtainable by you, but any information or knowledge in the possession of or obtainable by your attorneys, investigators, adjusters, insurance carrier, representatives, agents, or anyone acting on your behalf or their behalf.

If you are unable to answer the question in full after exercising due diligence to secure the information to do so, answer as completely as possible and then explain the reason you are unable to answer more fully, and state the name, address (business and residence) of any person or persons able to supply the information.

If you determine that any question is not applicable, and consequently deserves no answer, state in detail why it is not applicable.

The term "you" or "your" refers to you, your agents, employees, investigators or anyone acting in your behalf.

The term "document(s)" includes all writings, recordings, photographs, motion pictures, electronic computer data storage, or other form of recordation or reproduction, whether original or copies.

INTERROGATORIES

1. Identify each person whom you expect to call as an expert witness at trial.

2. As to each person whom you expect to call as an expert witness at trial, state the subject matter on which the expert is expected to testify, the substance of the facts and the opinions to which the expert is expected to testify, and a summary of the grounds for each opinion.

Dated this 14 day of February 1992, at Claremont, California.

SHERNOFF, BIDART
& DARRAS

By: /s/ Frank N. Darras
FRANK N. DARRAS
Attorneys for Plaintiffs

**PROOF OF SERVICE**

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address-is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On FEB. 14 1992, I served the foregoing document described as:

SECOND SET OF INTERROGATORIES PROPOUNDED TO USAA

on all interested parties in this action:

[ ] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[X] by placing [ ] the original [X] a true copy

thereof enclosed in sealed envelopes addressed as follows:

Paul R. Fine, Esq.
Daniels, Baratta & Fine
1801 Century Park East
Ninth Floor
Los Angeles, California
90067
(213) 556-7900
FAX: (213) 556-2807

Attorneys for Defendant
UNITED SERVICES
AUTOMOBILE
ASSOCIATION

---

[X] BY MAIL

I caused such envelope to be deposited in the mail at Claremont, California. The envelope was mailed with postage thereon fully prepaid. I am "readily familiar" with this firm's practice of collection and processing correspondence for mailing. It is deposited with U.S. Postal service on that same day in the ordinary course of business. I am aware that on motion of party served, service is presumed invalid if postal cancellation

date or postage meter date is more than 1 day after date deposit for mailing in affidavit.

[ ] BY PERSONAL SERVICE

I caused to be delivered by hand to the above-listed addressees or to the addressees on the list attached hereto.

[ ] BY OVERNIGHT MAIL/COURIER

To expedite the delivery of the above-named document, said document was sent via overnight courier for next day delivery to:

[ ] BY FACSIMILE ("FAX")

In addition to the manner of proof of service indicated above, a copy was sent by FAX to:

[ ] (State) I declare under penalty of perjury under the laws of California that the above is true and correct.

[X] (Federal) I declare that I am employed in the office of a member of the bar of this court at those [sic] direction the service was made.

Executed on FEB. 14 1992, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

AO 88 (Rev 11/91) Subpoena in a Civil

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

LAUGHLIN E. WATERS, et al.

V.

UNITED SERVICES AUTOMOBILE ASSOCIATION

**SUBPOENA IN A CIVIL CASE**

CASE NUMBER:
CV 91 3615 WFN

TO: Custodian of Records
United Services Automobile Association
9800 Fredericksburg Road
USAA Building, San Antonio, Texas 78288
(512) 498-2211

[ ] YOU ARE COMMANDED to appear in the United States District Court at the place, dated, and time specified below to testify in the above case.

PLACE OF TESTIMONY ) COURTROOM
)
) _____
) DATE AND TIME
)

[ ] YOU ARE COMMANDED to appear at the place, date, and time specified below to testify at the taking of a deposition in the above case.

| PLACE OF DEPOSITION | DATE AND TIME |
|---|---|
| | |

[X] YOU ARE COMMANDED to produce and permit inspection and copying of the following documents or objects at the place, date, and time specified below (list documents or objects):

* * * SEE ATTACHMENT "1" * * *

| PLACE | DATE AND TIME |
|---|---|
| APPEARANCE NOT REQUIRED. MAIL COPIES TO:<br><br>Shernoff, Bidart & Darras<br>600 South Indian Hill Boulevard<br>Claremont, California 91711 | MARCH 5, 1992 |

[ ] YOU ARE COMMANDED to permit inspection of the following premises at the date and time specified below.

| PREMISES | DATE AND TIME |
|---|---|
| | |

Any organization not a party to this suit that is subpoenaed for the taking of a deposition shall designate one or more officers, directors, or managing agents, or other persons who consent to testify on its behalf, and may set forth, for each person designated, the matters on which the person will testify. Federal Rules of Civil Procedure, 30(b)(6).

| ISSUING OFFICER SIGNATURE AND TITLE (INDICATE IF ATTORNEY FOR PLAINTIFF OR DEFENDANT) | DATE |
|---|---|
| /s/ Frank N. Darras<br>FRANK N. DARRAS,<br>Attorneys for Plaintiffs | FEB. 14 1992 |

| ISSUING OFFICER'S NAME ADDRESS AND PHONE NUMBER | |
|---|---|
| 600 S. Indian Hill Blvd.<br>Claremont, CA 91711 | FRANK N. DARRAS, ESQ.<br>SHERNOFF, BIDART<br>& DARRAS<br>(714) 621-4935 |

ATTACHMENT "1"

DEFINITION

(1) The term "writings" refers to all writings as defined in Federal Rules of Evidence, rule 1001.

DOCUMENTS

1. All declarations or affidavits filed on behalf of USAA in each and every case listed in attached Exhibit "A", pertaining to the issue of jurisdiction in each respective court action.

2. All inter office memos, correspondence, memoranda or writings by USAA or any employee of USAA in each and every case listed in attached Exhibit "A", pertaining to the issue of jurisdiction in each respective court action.

## CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of February, 1992, I caused to be served one copy of the foregoing Appendix to Petition For A Writ Of Mandamus Or Other Appropriate Relief by hand upon:

William M. Shernoff, Esq.
Shernoff, Bidart & Darras
600 South Indian Hill Boulevard
Claremont, California 91711-5498

Clerk of the Court
United States District Court for
the Central District of California
312 North Spring Street
Los Angeles, California 90012

and by Federal Express upon:

The Honorable Wm. Fremming Nielsen
United States District Court for the
Eastern District of Washington
938 United States Courthouse
Spokane, Washington 99210-2208

/s/ Laurie F. Calder
Laurie F. Calder, Esq.

Counsel for Petitioner
United Services
Automobile Association

WILLIAM M. SHERNOFF, #38856
MICHAEL J. BIDART, #60852
FRANK N. DARRAS, #128904
GARY L. TYSCH, #128389
D. SCOTT MOHNEY, #124426
Members of the Firm
SHERNOFF, BIDART & DARRAS
600 South Indian Hill Boulevard
Claremont, California 91711-5498
(714) 621-4935

Attorneys for Plaintiffs

UNITED STATES DISTRICT COURT

CENTRAL DISTRICT OF CALIFORNIA

| | |
|---|---|
| LAUGHLIN E. WATERS AND VOULA D. WATERS, Plaintiffs, v. UNITED SERVICES AUTOMOBILE ASSOCIATION, Defendant. | Case No. CV-91-3615-WFN<br><br>FORMAL REQUEST FOR DISCOVERY AND PRODUCTION OF DOCUMENTS AND THINGS FOR INSPECTION, COPYING OR PHOTOGRAPHING PURSUANT TO FEDERAL RULES OF CIVIL PROCEDURE, RULE 34 |

DEMANDING PARTY: Plaintiffs, LAUGHLIN E. WATERS and VOULA D. WATERS

RESPONDING PARTY: Defendant, UNITED SERVICES AUTOMOBILE ASSOCIATION

SET NO.: TWO

TO THE DEFENDANT, UNITED SERVICES AUTOMOBILE ASSOCIATION ("USAA"), AND TO ITS ATTORNEYS OF RECORD:

Pursuant to the Federal Rules of Civil Procedure, rule 34, plaintiffs hereby formally demand production and inspection of the following documents at the hour of 10:00 a.m. on ___, 1992, at the office of Plaintiff's attorneys located at 600 South Indian Hill Boulevard, Claremont, California.

The manner of inspection shall be personal inspection including the copying or photographing by or on behalf of the plaintiffs the below-mentioned documents, and other tangible things. If you withhold any documents requested because you claim a privilege, state the privilege claimed for each and every document, describe each document by its author, describe the name and occupation of the author, describe the name and occupation of each recipient, date of issuance, who, if anyone, received a copy of the document, and its general subject matter, including a brief description of the nature and context. Please number the documents produced sequentially to conform with the order in which the documents are maintained in your files.

A personal appearance by defendant and/or counsel is not required if defendant will submit copies of the documents described below with their verification, executed under penalty of perjury, verifying that the copies provided are accurate and true copies of the complete records requested.

PLEASE NOTE: Federal Rules of Civil Procedure, rule 34(b) requires two acts for compliance with this request:

(1) Service of a written response under oath within 30 days; and

(2) Production of documents or tangible things on or before the date of production specified above.

## DEFINITION

(1) The term "writings" refers to all writings as defined in Federal Rules of Evidence, rule 1001.

## DOCUMENTS REQUESTED

1. All writings, including correspondence, from USAA to USAA's counsel of record in each and every case listed in attached Exhibit "A", pertaining to the issue of jurisdiction in each respective court action.

2. All writings, including correspondence, from USAA's counsel of record to USAA in each and every case listed in attached Exhibit "A", pertaining to the issue of jurisdiction in each respective court action.

3. As referenced on page 11 of defendant's Opposition to Request for Sanctions, "the internal memorandum to all senior claims attorneys, claims attorneys, supervisors of litigation, regional claims management, and casualty file handlers reminding them that 'USAA shall appear neither as a plaintiff nor defendant in federal court when diversity is the jurisdictional basis' " and any prior drafts of the internal memorandum.

4. As referenced on page 11 of defendant's Opposition to Request for Sanctions, "the memorandum from its General Counsel to all of its approximately 3,200 outside counsel advising them that '[u]nder no circumstances should any case involving USAA be commenced in, defended in, or removed to federal court on the basis of diversity jurisdiction' ", and any prior drafts of the memorandum.

5. As referenced on pages 11 and 12 of defendant's Opposition to Request for Sanctions, the "special notice to its new case file forms specifying that 'USAA, a reciprocal interinsurance exchange, as an entity, is not subject to federal diversity jurisdiction in any of the federal district' ", and any prior drafts of the special notice.

6. As referenced on page 12 of defendant's Opposition to Request for Sanction, any and all documents, writings, memorandums, or manuals evidencing that USAA "updated its internal docketing procedures and investigated available computer software to enable it to better track all pending court cases."

7. As referenced in the Report on Measures Undertaken to Insure that United Services Automobile Association, as an Entity, will not be a Party in Federal Court Actions Based on Diversity of Citizenship ("the report"), the bulletin that was sent by USAA to "all regional claims officials . . . in the various USAA offices advising them of the diversity issue", and any prior drafts of the bulletin.

8. As referenced in the report, the December 12, 1988 memorandum sent by USAA to all senior claims attorneys, supervisors of litigation, and San Antonio claims counsel staff, and any prior drafts of the bulletin.

9. any and all documents or writings distributed by USAA at, or prepared by USAA for use at the May 10, 1989 legal conference for senior claims attorneys, supervisors of litigation, and regional claims management personnel, as referenced in the report.

10. As referenced in the report, the September 6, 1900 USAA memorandum "addressing the issue to all senior claims attorneys, claim attorneys, supervisors of litigation, regional claim management, and casualty file handlers", and any prior drafts of the memorandum.

11. As referenced in the report, the November 8, 1990 memorandum from USAA's Senior Vice President and General Counsel to all of USAA's approximately 3,200 outside counsel, and any prior drafts of the memorandum.

12. As referenced in the report, the November 14, 1990 attachment, to be included in the USAA Litigation Manual, which explains the diversity problem with respect to USAA, and any prior drafts of the attachment.

13. As referenced in the report, the USAA litigation manual section dealing with diversity or jurisdiction, including all revisions, additions, modifications, or deletions from 1980 to the present.

14. As referenced in the report, the November 20, 1990 revised transmittal memorandum, and any prior drafts of the memorandum.

DATED this 24 day of March, 1992, at Claremont California.

SHERNOFF, BIDART & DARRAS

By: /s/ Frank N. Darras
FRANK N. DARRAS
Attorneys for Plaintiffs

**PROOF OF SERVICE**

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the county of Los Angeles, State of California. I am over the age of 18 and not a party to the within action; my business address is: 600 South Indian Hill Boulevard, Claremont, California 91711.

On MAR. 24 1992, I served the foregoing document described as:

DEMAND FOR PRODUCTION OF DOCUMENTS
Set No. 2
Propounded to: USAA
Propounded by: Plaintiffs

on all interested parties in this action:

[X] by placing [ ] the original [X] a true copy

thereof enclosed in sealed envelopes addressed as stated on the attached mailing list.

[ ] by placing [ ] the original [ ] a true copy

thereof enclosed in sealed envelopes addressed as follows:

[X] BY MAIL

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[X] (Federal) I declare that I am employed in the office of a member of the bar of this

court at whose direction the service was made.

Executed on MAR. 24 1992, at Claremont, California.

/s/ Jo-Ann Shimizo
JO-ANN SHIMIZO

**PROOF OF SERVICE LIST**

*Waters v. USAA*
Federal (91-3615WFN)

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IN THE
UNITED STATES COURT OF
APPEALS FOR THE NINTH CIRCUIT

UNITED SERVICES AUTOMOBILE ASSOCIATION,

*Petitioner,*

v.

UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA,

*Respondent,*

and

LAUGHLIN E. WATERS AND VOULA D. WATERS,

*Real Parties in Interest.*

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PETITION FOR WRIT OF MANDAMUS
OR OTHER APPROPRIATE RELIEF
TO THE UNITED STATES DISTRICT COURT
FOR THE CENTRAL DISTRICT OF CALIFORNIA

---

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IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

| | |
|---|---|
| UNITED SERVICES AUTOMOBILE ASSOCIATION, *Petitioner,* | ) |
| v. | ) |
| UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA, *Respondent,* | ) |
| and | ) |
| LAUGHLIN E. WATERS AND VOULA D. WATERS, *Real Parties in Interest.* | ) |

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PETITION FOR A WRIT OF MANDAMUS OR OTHER APPROPRIATE RELIEF TO THE UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA

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## STATEMENT OF ISSUES PRESENTED

1. Whether the district court committed clear legal error in holding, contrary to the decision of the Supreme Court in *Carden v. Arkoma Assocs.*, 494 U.S. 185 (1990), and decisions of this Court and other circuits, that it should apply a "functional" approach in determining the citizenship of a non-corporate entity for diversity purposes.

2. Whether this case otherwise satisfies the standards for issuance of a writ of mandamus.

## STATEMENT OF RELIEF SOUGHT

USAA seeks a writ of mandamus directing the United States District Court for the Central District of California to dismiss the complaint in *Waters v. United Services Automobile Ass'n*, Civ. No. 91-3615 (C.D. Cal.).

## INTRODUCTION

Pursuant to 28 U.S.C. § 1651 (1988) and Rule 21 of the Federal Rules of Appellate Procedure, petitioner USAA requests this Court to issue a writ of mandamus or other appropriate relief to the United States District Court for the Central District of California. On February 7, 1992, that court (Judge Wm. Fremming Nielsen) denied USAA's motion to dismiss this case for lack of subject matter jurisdiction, and today denied USAA's motion to certify an interlocutory appeal pursuant to 28 U.S.C. § 1292(b). USAA seeks a writ directing the court to dismiss the action.[1]

This case involves the thus far successful effort of a sitting federal judge, Hon. Laughlin E. Waters, as plaintiff in this action, to improperly invoke the diversity jurisdiction of his own federal court, the United States District Court for the Central District of California. Judge Waters

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[1] Simultaneously herewith petitioner is filing an Emergency Motion under Circuit Rule 27-3 to Stay Proceedings Pending Review.

also seeks to sanction the petitioner/defendant USAA, a reciprocal inter-insurance exchange, which is licensed in Texas but has members in every state, for moving to dismiss the case on jurisdictional grounds. Judge Waters' sanctions motion is still pending in the district court.

All of the sitting federal judges in the Central District having disqualified themselves, on September 9, 1991, the Chief Judge of this Circuit appointed Judge Nielsen from the Eastern District of Washington to hear this case. In agreeing with the plaintiff Waters that he may keep his case in federal court, the court below has rendered a decision directly inconsistent with a recent decision of the United States Supreme Court, with a decision of this Court, and with decisions of the Second and Tenth Circuits holding with respect to this very defendant that federal diversity jurisdiction is not available.

In *Carden v. Arkoma Assocs.*, 494 U.S. 185, 195 (1990), the Supreme Court rejected a functional approach to determining an artificial, unincorporated entity's jurisdictional status, holding instead that courts should, " 'without analysis of the particular entity before [them], count every member of an unincorporated association for purposes of diversity jurisdiction' " (citation omitted). Both this Court and the Fifth Circuit have also applied *Carden*'s general rule. *See Rockwell Int'l Credit Corp. v. United States Aircraft Ins. Group*, 823 F.2d 302, 304 (9th Cir. 1987) ("All members of an unincorporated association must be diverse from the opposing party."); *Newport Ltd. v. Sears, Roebuck & Co.*, 941 F.2d 302, 306 (5th Cir. 1991) (refusing to apply a "characteristic-by-characteristic inquiry" to a Louisiana limited partnership), *cert. denied*, 1992 U.S. LEXIS 1299 (U.S. 1992). Moreover, the Second Circuit in

*Baer v. United Services Auto. Ass'n*, 503 F.2d 393, 396 (2d Cir. 1974), and the Tenth Circuit in *Tuck v. United Services Auto. Ass'n*, 859 F.2d 842, 845 (10th Cir. 1988), *cert. denied*, 489 U.S. 1080 (1989), have held that, under Texas law, USAA is an unincorporated association and thus a citizen of every state in which it has members.

In *Tuck*, The Tenth Circuit further observed that, on a number of occasions, USAA had sued, or permitted itself to be sued, in diversity, even after the Second Circuit's decision in *Baer*. Indicating that it disapproved of USAA's appearing in federal diversity actions, the court warned that it "expect[ed]" USAA to file motions to dismiss "in all pending diversity litigation." *Id.* at 845. n.3.[2]

The decision below puts petitioner in the unenviable and untenable position of having been directed by the Tenth Circuit to dismiss all diversity actions from federal court at the same time that the court below has ordered petitioner to proceed in federal court and threatened to sanction petitioner for, in essence, complying with the Tenth Circuit's direction.

## STATEMENT OF FACTS

1. On July 5, 1991, plaintiffs, Judge Laughlin E. Waters and his wife, Voula D. Waters, filed suit against

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[2] Since the Tenth Circuit's 1988 decision in *Tuck*, USAA has taken, and continues to take, numerous measures designed to ensure that it no longer participates in federal diversity cases. Among other actions, USAA has issued a series of memoranda to inside and outside counsel warning them to stay out of federal court and has asked counsel to identify any federal diversity cases in which USAA appears as a party.

USAA in the United States District Court for the Central District of California.[3] The Waters alleged that USAA had breached its duty of good faith and fair dealing under a homeowner's insurance policy by failing to offer adequate reimbursement for the damages that their home had sustained in a fire. The Waters complained that USAA had "unreasonably delay[ed] payments to [them]" in refusing to accept a $442,663.35 bid for repair work by their contractor, TMLC Construction Services Co. ("TMLC") (plaintiffs' claim apparently being that USAA should have agreed to have the work undertaken by their son, Laughlin E. Waters Jr., an Executive Vice President of that Company). Cpl. ¶¶ 11, 25(b) (Tab 3). They further argued that USAA's contractor's bid of $319,019.38 was "meaningless" and indicative of USAA's " 'low bid' estimating approach," Cpl. ¶¶ 13, 14 (Tab 3), and that, as a result of USAA's "unreasonable and bad faith conduct," they had suffered both economic damages and "anxiety, worry, mental and emotional distress," Cpl. ¶¶ 26, 27 (Tab 3). The Waters sought economic, consequential, and punitive damages for the "cruel and unjust hardship" that they had endured. Cpl. ¶ 29 (Tab 3).

Pursuant to its post-*Tuck* policy of avoiding all federal diversity litigation, USAA sought to have the Waters voluntarily dismiss their complaint from federal court, pointing to the decision in *Tuck*. That effort having been unavailing, on July 26, 1991, USAA promptly moved to

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[3] Copies of the complaint and other relevant pleadings in the district court are submitted herewith in a separate Appendix. References to those documents herein will identify their names and Appendix tab numbers.

dismiss the Waters' complaint on the ground that the matter belonged in state court. On October 15, 1991, the Waters opposed USAA's motion and requested that the district court award sanctions in the amount of $1.72 million. The theory of the Waters' sanctions motion is far from clear. Initially, they appeared to complain that petitioners' seeking to dismiss the action was improper. *See* Pl. Opp. at 3 (Tab 5). Forced ultimately to concede that a motion to dismiss was appropriate, the Waters then contended that USAA's motion, while citing *Tuck*, had somehow improperly failed to disclose USAA's past inconsistent positions on the issue and that the Waters, somehow acting as private attorneys general, could appropriately seek to punish USAA for its past behavior in other cases. See Pl. Supp. Opp. at 9-16 (Tab 10).[4] The Waters allowed that the government should receive some of the sanctions for wasting judicial resources on USAA in the past, but indicated that, "[n]aturally, the Waters should receive a portion of the sanctions award for their efforts in bringing the wrongdoer to account." *Id.* at 15-16 (Tab 10). Though they did not suggest that they had suffered any losses from USAA's prompt motion to dismiss their claim, the Waters proposed that the "award of sanctions be split between the U.S. Treasury and [them]." *Id.* at 16 (Tab 10).

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[4] It is, of course, well established that Rule 11 does not authorize the payment of sanctions to an opposing party where no misconduct has occurred in the case before the court. *See* Gregory Joseph, *Sanctions: The Federal Law of Litigation Abuse* § 5(D)(2)(c), at 71-72 (1989); *Soules v. Kauaians for Nukolii Campaign Comm.*, 849 F.2d 1176, 1185 (9th Cir. 1988).

2. On February 7, 1992, the district court denied USAA's motion to dismiss and continued under advisement the Waters' motion for sanctions. First, the district court declined to apply the Supreme Court's holding in *Carden v. Arkoma Associates*, 494 U.S. 185, 195-96 (1990), that "diversity jurisdiction in a suit by or against [an artificial] entity depends on the citizenship of 'all the members.' " (citation omitted). Instead, the court applied the Supreme Court's sixty-year-old decision in *Puerto Rico v. Russell & Co.*, 288 U.S. 476 (1933), which held that a Puerto Rican entity known as a *sociedad en comandita* could be treated as a citizen of Puerto Rico for purposes of determining federal court jurisdiction. Based on *Russell*, the district court determined that the question before it was "whether USAA has sufficient corporate traits to be within the *sociedad en comandita's* 'corporate' boundaries." Order at 3. Noting that "USAA is a statutory entity governed by very specific Texas insurance laws," and that, for a variety of purposes, "federal laws treat USAA in a corporate manner," the court answered that question in the affirmative. *See id.* at 4.

Next, the district court acknowledged that *Carden* appeared to prohibit courts from "look[ing] beyond the incorporated/unincorporated dichotomy and study[ing] the internal organization, state law requirements, management structure, and capacity or lack thereof to act and/or sue to determine diversity of citizenship." 494 U.S. at 190; *see* Order at 2-3. The court also conceded that the Supreme Court's decision in *United Steelworkers v. Bouligny*, 382 U.S. 145 (1965), which " 'considered and rejected applying *Russell* beyond its facts,' " Order at 3

(quoting *Carden*, 494 U.S. at 190 n.2), "appeared to undercut *Russell*." *id.* at 5. But the district court nonetheless concluded that "*Carden* makes it clear that *Russell* still has precedential value" and that *Russell*'s functional approach to determining an entity's jurisdictional status "must be considered in any analysis of an association as a juridical person." *Id.*

Finally, the district court stressed that it was "not unmindful" that the Second Circuit in *Baer v. United Services Auto. Ass'n* and the Tenth Circuit in *Tuck v. United Services Auto. Ass'n* had reached contrary conclusions about USAA's status for diversity purposes. *See id.* at 5. The court purported to distinguish these cases, however, on the grounds that they were "pre-*Carden*, relied on *Bouligny* and did not discuss *Russell*." *id.* On February 7, 1992, the court also ordered discovery on the sanctions issue and the merits of the Waters' claims, set a May 11, 1992, date for a hearing on the sanctions motion, and a September 14, 1992 date for a trial on the merits.

On February 11, 1992, USAA filed a motion in the district court seeking certification of the Order pursuant to 28 U.S.C. § 1292(b) (1988) and a stay of discovery. The Waters opposed both motions on February 25, 1992. In their opposition, the Waters argued that USAA's request for permission to appeal should be denied because USAA's effort to seek interlocutory review was somehow inappropriate. They urged that USAA's motion was "a slap in the face to the Ninth Circuit," Pl. Cert. Opp. at 1 (Tab 15), and a "cunning effort to waste . . . judicial time and resources," *id.* at 2 (Tab 15), which is "outrageous, unjustifiable and itself a basis for sanctions," *id.* at 4 (Tab

15).[5] The plaintiffs did not cite *Carden* in their opposition or explain how the district court's position could possibly be consistent with that case. The district court denied USAA's certification and stay motions on February 28, 1992, and reset the sanctions hearing for May 14 and the trial for June 22, 1992. The court ordered that USAA begin producing material in response to discovery by March 16, 1992. (The text of the court's latest order has not yet been released.)

## ARGUMENT

Although a writ of mandamus is an extraordinary remedy, it may in certain circumstances, serve as " 'an expeditious and effective means of confining the inferior court to a lawful exercise of its prescribed jurisdiction.' " *Mafnas v. United States District Court*, 919 F.2d 101, 103 (9th Cir. 1990), *appeal dismissed*, 936 F.2d 1068 (9th Cir. 1991) (quoting *People of Guam v. District Court*, 641 F.2d 816, 820 (9th Cir. 1981)). This Court consults five guidelines to determine whether mandamus is appropriate in a particular case:

1) whether the petitioner has no other means such as an appeal, to obtain the desired relief;

2) whether petitioner will be damaged or prejudiced in any way not correctable on appeal;

3) whether the district court is clearly erroneous as a matter of law;

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[5] The Waters also argued that "[t]his is a case where USAA 'low-balled' the wrong folks." *Id.* at 7 (Tab 15).

4) whether the district court's order is an oft repeated error or manifests a persistent disregard of the federal rules;

5) whether the district court's order raises new and important problems or issues of first impression.

*Mortgages, Inc. v. United States District Court*, 934 F.2d 209, 211 (9th Cir. 1991); *see Bauman v. United States District Court*, 557 F.2d 650, 654-55 (9th Cir. 1977). "No single factor is determinative, and all five factors need not be satisfied at once." *Valenzuela-Gonzalez v. United States District Court*, 915 F.2d 1276, 1279 (9th Cir. 1990) (internal citation omitted). Consultation of the five guidelines here confirms that USAA's petition warrants mandamus relief directing the district court to dismiss the complaint for want of jurisdiction.

## I. The District Court's Determination That USAA Should Be Treated As A Corporate Citizen Of The State Of Texas Was Clearly Erroneous As A Matter Of Law

" 'The traditional use of the writ in aid of appellate jurisdiction both at common law and in the federal courts has been to confine an inferior court to a lawful exercise of its prescribed jurisdiction or to compel it to exercise its authority when it is its duty to do so.' " *Mallard v. United States District Court*, 490 U.S. 296, 308 (1989) (citation omitted). The district court here refused to apply the Supreme Court's holding in *Carden v. Arkoma Associates*, 494 U.S. 185, 195 (1990), that a court should, " 'without analysis of the particular entity before it, count every member of an unincorporated association for purposes of

diversity jurisdiction.' " (Citation omitted). Instead, in exercising diversity jurisdiction over USAA, the court relied solely on the Supreme Court's sixty-year-old decision in *Puerto Rico v. Russell & Co.*, 288 U.S. 476 (1933). The Supreme Court's decisions in both *Carden* and *United Steelworkers v. Bouligny*, 382 U.S. 145 (1965), however, clearly foreclose the district court's reliance on *Russell*.

In *Russell*, the Supreme Court determined the citizenship of a *sociedad en comandita*, an entity organized under the civil code of Puerto Rico, in order to decide whether a case could be removed from a Puerto Rican court to federal court. *See* 288 U.S. at 477-78. Under the Organic Act of Puerto Rico, federal jurisdiction existed if parties on either side of a controversy were citizens of a foreign state or "citizens of a State, Territory or District of the United States not domiciled in Puerto Rico." *Id.* at 478. All members of the *sociedad* resided outside of Puerto Rico. The Court, however, determined that the *sociedad* itself, rather than its members, was the party to the action. The Court reached this conclusion only after examining the *sociedad*'s structure and operations and determining that the *sociedad* had a number of corporate-like attributes. Accordingly, because the Court decided to treat the *sociedad* as a corporate citizen of Puerto Rico, under whose laws it was organized, the Court held that the case could not be removed to federal court. *See id.* at 480-82.

The *Russell* Court made clear that its holding was limited to the peculiar facts of that case. Acknowledging that "[t]he tradition of the common law is to treat as legal persons only incorporated groups and to assimilate all others to partnerships," *id.* at 480 (citation omitted), the

Court then stated that "[t]he tradition of the civil law, *as expressed in the Code of Puerto Rico,* is otherwise," *id.* (emphasis added). After deciding to treat *sociedads* like corporations for jurisdictional purposes, the Court further emphasized that the effect of its holding was to contract federal jurisdiction because "non-residents of Puerto Rico, who ha[d] taken advantage of its laws to organize a juridical entity for the purpose of carrying on business there, [could no longer] remove from the [Puerto Rican courts] controversies arising under local law." *Id.* at 482.

Thus, by its own terms, *Russell* stands for the limited proposition that foreign, unincorporated civil-law entities may, in some cases, be treated like corporations for jurisdictional purposes. That *Russell*'s applicability is so limited was stated unambiguously in both *Bouligny* and *Carden.*

In *Bouligny,* the Supreme Court determined the citizenship for diversity purposes of an unincorporated labor association. The Court first acknowledged its longstanding rule that a corporation should be treated as a citizen of its incorporating State. *See* 382 U.S. at 148. But, the court noted that in *Chapman v. Barney,* 129 U.S. 677 (1889), it had declined to extend that rule to unincorporated entities – in that case, a joint stock company. *See id.* at 149. Next, the Court considered arguments that "many voluntary associations and labor unions are indistinguishable from corporations in terms of the reality of function and structure," *id.* at 150, but concluded that it was not the appropriate body to evaluate these policy

arguments. Thus, the Court held that the labor association's citizenship was that of each of its members. *See id.* at 150-53.

Twenty-five years later in *Carden*, the Court considered the citizenship of a limited partnership. The Court observed that in *Bouligny*, it had "reiterated that 'the doctrinal wall of *Chapman v. Barney*' would not be breached." 494 U.S. at 189 (citation omitted). Elaborating on *Bouligny*, the *Carden* Court held broadly that the "wide assortment of artificial entities," *id.* at 197, that "[t]he 50 States have created, and will continue to create," *id.*, must be measured by the citizenship of each of their members:

> In sum, we reject the contention that to determine for diversity purposes, the citizenship of an artificial entity, the court may consult the citizenship of less than all of the entity's members . . . . [Rather,] a suit by or against the entity depends on the citizenship of "all the members."

*Id.* at 195 (citation omitted); *see id.* at 199 (O'Connor, J., dissenting) (criticizing the majority's "newly formulated rule that the court will, without analysis of the particular entity before it, count every member of an unincorporated association for purposes of diversity jurisdiction.").

In explaining why it had rejected *Carden*'s bright-line rule in favor of *Russell*'s functional approach, the district court reached the untenable conclusion that "[in *Carden*,] the Supreme Court did not draw [a] black and white line of jurisdictional status simply based upon the label corporate or non-corporate entity," but, instead, "specifically distinguished" *Russell*. *See* Order at 2-3. The district court thus read *Carden* as standing for the exact opposite of its

clear holding. In the district court's view, *Carden* had not only endorsed *Russell*'s functional approach but had "ma[de] it clear" that *Russell* "must be considered in any analysis of an association as a juridical person." *See id.* at 5. The district court's conclusion completely misses the mark.

Neither *Bouligny* nor *Carden* endorsed the *Russell* Court's functional approach to determining an entity's jurisdictional status. The *Bouligny* Court explicitly stated that "*Russell* does not furnish [a] precedent" for courts to analyze the structure and operations of a wide array of unincorporated, artificial entities. *See* 382 U.S. at 151. On the contrary, the Court stressed, all "pleas for extension of the diversity jurisdiction to hitherto uncovered broad categories of litigants ought to be made to the Congress and not to the courts." *Id.* at 150-51. In *Carden*, the Court flatly rejected the argument that *Russell*

> "reflec[ts] the Supreme Court's willingness to look beyond the incorporated/unincorporated dichotomy and to study the internal organization, state law requirements, management structure, and capacity or lack thereof to act and/or sue, to determine diversity of citizenship."

494 U.S. at 190 (citation omitted). "The problem with this argument lies not in its logic," according to the Court, "but in the fact that the approach it espouses was proposed and specifically rejected in *Bouligny*." *Id.*

Indeed, read together, both *Bouligny* and *Carden* have expressly limited *Russell's* applicability to entities formed under civil law. In *Bouligny*, the Court stressed that "[t]he problem which [*Russell*] presented was that of fitting an exotic creation of the civil law, the *sociedad en comandita*,

into a federal scheme which knew it not." 382 U.S. at 151. The *Carden* Court expanded on *Bouligny's* explanation, holding that:

> There could be no doubt, after *Bouligny*, that at least all common-law entities (and likely all entities beyond the Puerto Rican *sociedad en comandita*) would be treated for purposes of the diversity statute pursuant to what *Russell* called "[t]he tradition of the common law," which is "to treat as legal persons only incorporated groups and to assimilate all others to partnerships."

494 U.S. at 190; *see id.* at 208-09 (O'Connor, J., dissenting) (criticizing majority's "holding that an association within the continental United States is not afforded the same treatment as its virtually identical Puerto Rican counterpart"). The district court's conclusion that *Russell*, although "undercut" by *Bouligny*, was somehow revived in *Carden* is thus wholly unfounded. *Carden* states clearly that outside the civil law context – and "likely" beyond its peculiar facts – *Russell* has no precedential effect.

Controlling law in this Circuit also requires that USAA's citizenship be determined by *Carden's* and *Bouligny's* bright-line rule rather than by *Russell's* functional approach. This Court has consistently acknowledged the general rule that the citizenship of unincorporated associations is determined by the citizenship of their members. In *Rockwell Int'l Credit Corp. v. United States Aircraft Ins. Group*, 823 F.2d 302, 303-04 (9th Cir. 1987), for example, a "group of independent insurance companies" relied on diversity jurisdiction to remove a case to federal court. This Court raised the

jurisdictional issue sua sponte and held that since the insurance companies were operating as "an unincorporated association," the case must be dismissed for lack of subject matter jurisdiction because "[a]ll members of an unincorporated association must be diverse from the opposing party." *Id.* at 304; *accord Faysound Ltd. v. United Coconut Chems., Inc.*, 878 F.2d 290, 292 (9th Cir. 1989) (citing *Rockwell*); *O'Halloran v. Univ. of Wash.*, 856 F.2d 1375, 1381 (9th Cir. 1988) (citing *Rockwell*); *Otero v. Int'l Union of Elec., Radio & Machine Workers*, 474 F.2d 3, 4 (9th Cir. 1973) (per curiam) (citing *Bouligny*).[6] This Court has also recognized that *Russell* only applies to civil law entities. Indeed, in *Cohn v. Rosenfeld*, 733 F.2d 625, 628-29 (9th Cir.), *cert. denied*, 469 U.S. 932 (1984), this Court emphasized the *Russell* Court's distinction between " 'the tradition of the common law' . . . [and] the more diverse tradition of the civil law as expressed in the Code of Puerto Rico," *id.* at 628-29 (citation omitted), before applying *Russell* to the civil-law entity at issue in that case (an anstalt organized under the laws of Liechtenstein, a civil law country).

That *Russell* lacks any precedential force in the present context is made even more clear in the Fifth Circuit's recent decision in *Newport Ltd. v. Sears, Roebuck & Co.*, 941 F.2d 302 (5th Cir. 1991), *cert. denied*, 1992 U.S. LEXIS 1299 (U.S. 1992). In *Newport Ltd.*, the court decided the citizenship for diversity purposes of Newport Limited, a Louisiana partnership in commendam. Pointing out the parallel

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[6] *Rockwell* was subsequently overruled "to the extent that [it] authorize[d] sanctions on appeal under Rule 11." *Partington v. Gedan*, 923 F.2d 686, 688 (9th Cir. 1991) (per curiam).

civil-law origins of the Puerto Rican *sociedad en comandita* and the Louisiana partnership in commendam, Sears had argued that, like the *sociedad*, the Louisiana partnership should be treated as a juridical person. The Fifth Circuit disagreed, noting that "*Carden* . . . essentially forecloses the characteristic-by-characteristic inquiry which Sears would have us undertake today." *Id.* at 306. The Fifth Circuit further concluded:

> We must agree with the observation of the trial court "that Louisiana, while enjoying a civilian tradition, is one of the United States. The fact that a Louisiana partnership in commendam derives from a civilian code provides no other reason for treatment different from other American limited partnerships." *We find little support for the suggestion that [in Russell] the Supreme Court intended an exception for any entity other than a sociedad en comandita,* especially for one which on its face is indistinguishable from an ordinary limited partnership.

*Id.* at 307 (citation omitted) (emphasis added in part); *see also Temple Drilling Co. v. Louisiana Ins. Guar. Ass'n*, 946 F.2d 390, 394 (5th Cir. 1991) (observing that in *Carden*, the Supreme Court rejected the argument that "*Russell* reflects the Court's willingness to look behind the incorporated/unincorporated dichotomy" in some cases).[7]

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[7] Other courts, including a judge in the Central District of California, have also construed *Carden* broadly. *See, e.g., Danjag, S.A. v. MGM/UA Communications Co.*, 773 F. Supp. 194, 198 (C.D. Cal. 1991) ("In *Carden*, the Supreme Court noted that the corporation remains *the one artificial entity* in our law whose citizenship, for jurisdictional purposes, is determined without

(Continued on following page)

Finally, with respect to USAA in particular, two courts of appeals have already held that, for diversity purposes, USAA's citizenship is that of its members. In *Baer v. United Services Auto. Ass'n*, 503 F.2d 393, 395 (2d Cir. 1974), the Second Circuit found the "formal distinction drawn between the insurance reciprocal and the insurance corporation under state law . . . dispositive on the issue of whether the reciprocal should be considered a corporation for diversity purposes." The Tenth Circuit, in *Tuck v. United Services Auto. Ass'n*, 859 F.2d 842 (10th Cir. 1988), *cert. denied*, 489 U.S. 1080 (1989), likewise held that it lacked diversity jurisdiction over USAA because " 'the citizenship of an unincorporated association is the citizenship of the individual members of the association.' " *Id.* at 844. (citation omitted) Indeed, since the Supreme Court decided *Carden*, all of the other courts that have ruled on USAA's jurisdictional status have held that they cannot exercise diversity jurisdiction over claims involving USAA. *See, e.g., Pennington v. Hartford Casualty Ins. Co. (and United Services Auto. Ass'n)*, No. 91-614-S (E.D. Okla. Jan. 29, 1992); *Byrne v. USAA Property & Casualty Ins. Co.*, Civ. No. 91-2028 (E.D. Pa. July 18,

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reference to the identity or character of its owners") (emphasis added); *Penteco Corp. v. Union Gas Sys., Inc.*, 929 F.2d 1519, 1523 (10th Cir. 1991) (noting that "*Carden* held that for entities other than corporations (and sometimes trusts), diversity jurisdiction . . . depends on the citizenship of 'all the members' ") (citation omitted); *RLI Ins. Co. v. United States Aviation Underwriters*, 739 F. Supp. 1219, 1221 (N.D. Ill. 1990) (noting that in *Carden*, "the Supreme Court held that the citizenship of every member of an unincorporated entity must be considered for diversity purposes.").

1991); *Liberty Mutual Ins. Co. v. Brasby & United Services Auto. Ass'n*, Civ. No. 90-8447 (S.D. Fla. Apr. 30, 1991).[8]

Accordingly, both controlling Supreme Court and Ninth Circuit precedent, and persuasive authority in other circuits dictate that because USAA is an unincorporated entity that is not a creature of civil law, its citizenship for diversity purposes is the citizenship of each of its members. The district court's contrary holding flies in the face of this binding and unambiguous authority. This Court thus should issue a writ of mandamus to correct the district court's clearly erroneous jurisdictional determination. *See. e.g., Borja v. United States District Court*, 919 F.2d 100, 101 (9th Cir. 1990) (holding that mandamus was appropriate because a statute had eliminated the lower court's jurisdiction over the case); *Mafnas v. United States District Court*, 919 F.2d at 102 (same); *People of Guam v. District Court*, 641 F.2d at 820-21 (same).

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[8] In their opposition to USAA's certification and stay motions in the district court, the Waters argued that USAA's jurisdictional status did not present "simply 'a question of law' " because "the issue of jurisdiction has an inherent factual underpinning." Pl. Cert. Opp. at 4-5 (Tab 15). Similarly, they contended that other courts that have ruled on "the jurisdictional issue" have not considered "the effect of the changes in Texas corporation law which expressly defines a reciprocal insurance exchange as a corporation." *Id.* at 6 (Tab 15). As USAA pointed out in its Supplemental Brief In Support Of Its Motion To Dismiss in the district court, however, the current Texas statutes clearly distinguish between corporations and reciprocal inter-insurance exchanges. *See* Def. Supp. Br. at 5-14 (Tab 11). Moreover, the district court's opinion does not declare *Carden* inapplicable because USAA is a corporation under Texas law, but, instead, because USAA has a "corporate-like personality." *See* Order at 4.

## II. Mandamus Is Appropriate Because The District Court's Erroneous Order Could Adversely Affect The Efficient Operation Of The District Courts

Mandamus is particularly necessary in this case because the district court's erroneous holding could significantly disrupt the administration of justice in this Circuit. In *Arizona v. United States District Court (In re Cement Antitrust Litig.)*, 688 F.2d 1297, 1303-04 (9th Cir. 1982), *aff'd for lack of quorom*, 459 U.S. 1191 (1983), this Court explained that mandamus relief is often appropriate when the challenged order "implicate[s] the duty of appellate courts to exercise supervisory control of the district courts in order to insure proper judicial administration." Accordingly, since *In re Cement*, this court has not hesitated to issue writs of mandamus under its supervisory authority. In *Mortgages, Inc. v. United States District Court*, 934 F.2d 209 (9th Cir. 1991), for example, qui tam plaintiffs in a False Claims Act action sought a writ of mandamus ordering the district court to dismiss counterclaims filed against them. The Court observed:

> [T]he issue of whether counterclaims may be filed against qui tam plaintiffs is one that may confront a number of district court judges. In 1986, Congress substantially amended the FCA with the intent of encouraging such actions. At least one commentator has indicated these amendments will result in an increased filing of FCA lawsuits. A ruling from this court on this issue at this time will increase the efficient operation of the district courts.

*Id.* at 212 (citation omitted). After determining that the district court's denial of petitioners' motion to dismiss

was clearly erroneous, this Court granted the petitioners' request for a writ of mandamus. *See also Valenzuela-Gonzalez v. United States District Court*, 915 F.2d at 1279 (mandamus was appropriate, in part, because legal error was "likely to be 'oft-repeated' "); *City of Las Vegas v. Foley*, 747 F.2d 1294, 1296 (9th Cir. 1984) (granting petition for mandamus, in part, because resolution of a discovery dispute "would substantially aid the administration of justice").

This case is the quintessential candidate for this Court's exercise of its supervisory authority. The district court's decision, if allowed to stand, could have serious, adverse consequences on the efficient administration of this Circuit's district courts. The decision below has already created a conflict within this Circuit as to the appropriateness of applying a functional approach in determining the citizenship of non-corporate entities. *See* note 8 *supra*. Numerous district courts may determine the jurisdictional status of unincorporated entities before this Court has the opportunity to review the district court's jurisdictional determination in this case. Indeed, with more than 15,000 cases on its docket, USAA itself may soon have its jurisdictional status determined again by a number of district courts in the Circuit.[9] Those courts that choose to endorse the district court's rationale in this case

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[9] Indeed, in *United Services Auto. Ass'n v. Hawaiian Ins. & Guar. Co.*, Civ. No. 84-0300 (D. Haw.), a defendant sought to vacate a final judgment in a diversity action commenced by USAA and an award of sanctions on the theory that the district court lacked diversity jurisdiction.

would subject many unincorporated associations, including USAA, to the plainly incorrect functional analysis that the district court espouses. The result would be the different treatment of like entities in different district courts and an inevitable increase in the numbers of appeals to this Court. A writ of mandamus in this case thus would prevent this unnecessary dedication of federal judicial resources to the resolution of state law claims that must be brought in state court.

## III. Mandamus Is Necessary To Prevent USAA From Suffering Harm That Could Not Be Redressed On Appeal

Finally, this Court should grant USAA's petition because mandamus is the only appropriate remedy for the district court's refusal to follow controlling precedent. "[T]o insure that mandamus, rather than some other form of relief, is the appropriate remedy[,]" this Court generally requires that "petitioners . . . demonstrate that they have no other adequate means of obtaining the relief desired and that they will be damaged in a way not correctable on appeal from final judgment." *In re Cement Antitrust Litigation*, 688 F.2d at 1301. USAA's petition satisfies both requirements. First, because the district court has denied USAA's section 1292 motion, USAA has no other means of obtaining interlocutory relief from the Order. *See, e.g., Valenzuela-Gonzalez v. United States District Court*, 915 F.2d at 1270. Moreover, absent interlocutory relief, USAA would be subject to conflicting legal requirements throughout the proceedings below and until this Court renders a final decision on appeal. With its voluminous docket, USAA should not be required to

function under an uncertain jurisdictional regime for such a protracted period of time.

Although this Court has generally rejected the " 'position that the costs of trying massive civil actions render review after final judgment inadequate,' " *In re Cement Antitrust Litigation*, 688 F.2d at 1303 (quoting *American Crystal Sugar Co. v. United States District Court (In re Sugar Antitrust Litigation)*, 559 F.2d 481, 484 (9th Cir. 1977)), it has also recognized that mandamus relief may be justified when a party will suffer hardship that is " 'substantially in excess of the usual inconvenience of an unnecessary trial.' " *Varsic v. United States District Court*, 607 F.2d 245, 252 (9th Cir. 1979) (quoting *Pacific Car & Foundry Co. v. Pence*, 403 F.2d 949, 953 (9th Cir. 1968)); see also *Washington Pub. Utils. Group v. United States District Court*, 843 F.2d 319, 325 (9th Cir. 1987) ("[m]andamus relief may be justified if a party will suffer severe prejudice, as the result of inevitable delay and increased costs in being forced to undergo an unnecessary trial that is not correctable on appeal."). The substantial prejudice to USAA of having to manage its 15,000-case docket without knowing whether it must submit to federal diversity jurisdiction more than satisfies this Court's injury requirement for mandamus relief.[10]

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[10] Moreover, where, as here, the district court's Order would seriously disrupt the efficient administration of justice in this Circuit, "the degree of injury to the petitioner is a less critical factor." *In re Cement Antitrust Litigation*, 688 F.2d at 1303; *see also Mortgages, Inc. v. United States District Court*, 934 F.2d at 211 (granting mandamus even though "the fact that the

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As the district court recognized, both the Second Circuit in *Baer v. United Services Automobile Ass'n*, 503 F.2d at 396, and the Tenth Circuit in *Tuck v. United Services Automobile Ass'n*, 859 F.2d at 845, have held that, under Texas law, USAA is an unincorporated association and thus a citizen of every state in which it has members. The *Tuck* court went even further, however. That court observed that, on a number of occasions, "USAA [had] appeared in federal courts under their diversity jurisdiction, even after the decision in *Baer*." *Id.* at 845 n.3. It then warned that: "Because USAA has apparently 'rediscovered' Baer . . . and asked us to dismiss this action for lack of subject matter jurisdiction, we expect it to make similar motions in all pending diversity litigation." *Id.* In addition, the court directed the district court to consider the need for sanctions against USAA and/or its attorneys for failing to file a motion to dismiss earlier in the proceedings. *See id.* at 846.

Although the parties ultimately settled the case in *Tuck*, USAA took numerous measures to comply with the Tenth Circuit's strongly-worded admonition. As the attached report details, USAA issued a series of memoranda to its claims attorneys, supervisors, and outside counsel notifying them of the *Tuck* decision and warning them in no uncertain terms to stay out of federal court in diversity litigation. *See Report On Measures Undertaken To Insure That United Services Automobile Association, As An*

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lower court's order [would] result in additional cost and unreasonable delay [ordinarily would] not demonstrate sufficient prejudice to warrant mandamus relief").

*Entity, Will Not Be A Party In Federal Court Actions Based On Diversity Of Citizenship* (submitted on December 10, 1990 to the United States Court of Appeals for the Tenth Circuit in connection with *Tuck v. United Service Auto. Ass'n*, Nos. 90-5009 et al.) (Tab 2). In an effort to manage its docket more closely, USAA asked all counsel to identify any federal diversity cases in which USAA continued to appear as a party. USAA further warned its attorneys to stay out of federal diversity litigation by including the topic, "USAA As A Defendant In Federal Court," in its legal conferences, placing inserts in its Litigation Manual, and including notices in case files sent to local counsel.

The district court's denial of USAA's motion to dismiss, however, once again introduces uncertainty into the law governing unincorporated associations, like USAA. Outside the Second and Tenth Circuits, attorneys representing USAA in potential diversity litigation must now either ignore the Tenth Circuit's direction to forego all federal diversity litigation, or acquiesce in the district court's holding here that such litigation is appropriate. Neither choice is tenable. *Cf. Christensen v. United States District Court*, 844 F.2d 694, 697 (9th Cir. 1988) (granting mandamus where "[i]f Christensen and his attorney elected to defy the order [disqualifying the attorney] and then pursue a direct appeal, they would be subject to contempt sanctions and disciplinary action for ethical violations."). Moreover, parties opposing USAA in litigation will seize upon the district court's opinion as justification for improperly bringing or removing state law claims in the federal courts. These actions would substantially increase costs for all parties involved. Indeed, in

this case, it appears that the plaintiffs seek to take advantage of the costs to USAA of vindicating its jurisdictional position after trial, for they urge that having tried the matter in federal courts, "the likelihood that USAA would retry the entire action rather than settling is virtually nonexistent." Pl. Cert. Opp. at 5 (Tab 15). While USAA has no intention of abandoning its jurisdictional position, it should not be forced to undergo a useless trial in this matter to vindicate a position which is clearly correct.

Because it has been criticized harshly for acting inconsistently, USAA has an unusually compelling need for clear legal guidance from the federal courts. After *Carden*, this clear legal guidance existed until the court below decided single-handedly to resuscitate *Russell*. By correcting the district court's error of law on mandamus, this Court would ensure that USAA could continue consistently to adhere to its post-*Tuck* litigation policies (and therefore *Carden's* bright-line rule).

## CONCLUSION

For the foregoing reasons, USAA requests that this Court issue a writ of mandamus ordering the district court to dismiss the complaint in *Waters v. United Services Automobile Association*, Civ. No. 91-3615 (C.D. Cal.).

## STATEMENT OF RELATED CASES

USAA is unaware of any related case pending in this Court.

Respectfully submitted,

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*Counsel for Petitioner United Services Automobile Association*

February 28, 1992

## CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of February, 1992, I caused to be served one copy of the foregoing Petition For A Writ of Mandamus Or Other Appropriate Relief by hand upon:

William M. Shernoff, Esq.
Shernoff, Bidart & Darras
600 South Indian Hill Boulevard
Claremont, California 91711-5498

Clerk of the Court
United States District Court for
the Central District of California
312 North Spring Street
Los Angeles, California 90012

and by Federal Express upon:

The Honorable Wm. Fremming Nielsen
United States District Court for the
Eastern District of Washington
938 United States Courthouse
Spokane, Washington 99210-2208

/s/ Laurie F. Calder
Laurie F. Calder, Esq.

Counsel for Petitioner United
Services Automobile Association

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

| | | |
|---|---|---|
| UNITED SERVICES AUTOMOBILE ASSOCIATION, | ) | DOCKETED ORIGINAL 92-70122 |
| *Petitioner,* | ) | (Filed February 28, 1992) |
| v. | ) | |
| UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA, | ) | |
| *Respondent,* | ) | |
| and | ) | |
| LAUGHLIN E. WATERS AND VOULA D. WATERS, | ) | |
| *Real Parties in Interest.* | ) | |

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EMERGENCY MOTION UNDER CIRCUIT RULE 27-3
FOR A STAY PENDING REVIEW OF A
PETITION FOR A WRIT OF MANDAMUS
OR OTHER APPROPRIATE RELIEF

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CIRCUIT RULE 27-3 CERTIFICATE

I. The attorneys for the parties in this case are:

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II. Simultaneously with this Emergency Motion, United Services Automobile Association ("USAA") has filed a Petition For A Writ Of Mandamus Or Other Appropriate Relief requesting that this Court order the

United States District Court for the Central District of California to dismiss *Waters v. United Services Automobile Ass'n*, No. 91-3615 (C.D. Cal.), for lack of subject matter jurisdiction. Sitting by designation in the Central District of California, Judge Nielsen of the United States Court of Appeals for the Eastern District of Washington has ordered discovery in the case and USAA is currently required to file its initial discovery responses by March 16, 1992. USAA seeks this emergency stay to avoid having to participate in any district court proceedings in this case until this Court rules on USAA's Petition For A Writ Of Mandamus.

III. Earlier today, USAA notified counsel for the real parties in interest, the Clerk of the United States District Court for the Central District of California, and Judge Nielsen that USAA planned to file this Motion this afternoon. USAA has served copies of this Motion and the Petition (not including the appendix) by facsimile on the United States District Court for the Central District of California, counsel for the real parties in interest, and on Judge Nielsen. The Motion and Petition are also being hand-served on the United States District Court for the Central District of California and counsel for the real parties in interest, and served by Federal Express on Judge Nielsen.

## Corporate Disclosure Statement

None of United Services Automobile Association's subsidiaries or affiliates issues shares to the general public. However, the following mutual funds offered by USAA Investment Management Company trade on the

New York Stock Exchange: Aggressive Growth Fund; Growth Fund; International Fund; Gold Fund; Income Stock Fund (stocks); Income Fund (bonds); GNMA Certificates; Money Market Fund; Treasury Money Market Trust; Tax Exempt Money Market Fund; State Money Market Fund; High Yield Fund; Intermediate Term Fund; Short Term Fund; State Bond Fund; Cornerstone Fund; and Balanced Portfolio Fund.

IN THE
UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

UNITED SERVICES AUTOMOBILE ASSOCIATION,

*Petitioner,*

v.

UNITED STATES DISTRICT COURT FOR THE CENTRAL DISTRICT OF CALIFORNIA,

*Respondent,*

and

LAUGHLIN E. WATERS AND VOULA D. WATERS,

*Real Parties in Interest.*

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EMERGENCY MOTION UNDER CIRCUIT RULE 27-3
FOR A STAY PENDING REVIEW OF A
PETITION FOR A WRIT OF MANDAMUS
OR OTHER APPROPRIATE RELIEF

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Pursuant to Rules 8, 21, and 27 of the Federal Rules of Appellate Procedure and Section 1651 of Title 28 of the United States Code, petitioner United Services Automobile Association ("USAA") respectfully requests that this Court stay further proceedings in *Waters v. United Services Automobile Ass'n*, Civ. No. 91-3615 (C.D. Cal.), pending review and disposition of a Petition For A Writ Of Mandamus Or Other Appropriate Relief ("Petition") filed simultaneously herewith. A stay was sought in the district court and denied earlier today. Pursuant to Rule 27(a) of the Federal Rules of Appellate Procedure and Circuit Rule 27-3, USAA respectfully requests that this Court (a) request an immediate response to this motion from the real parties in interest and (b) rule on this motion on or before March 16, 1992, when petitioner must begin producing material in response to discovery in this case. The grounds to support of this motion, which were all submitted to the district court, are as follows:

1. Petitioner USAA is a reciprocal inter-insurance exchange, which is licensed in the State of Texas but has members in every State.

2. On July 5, 1991, plaintiffs, Hon. Laughlin E. Waters, a sitting judge on the United States District Court for the Central District of California, and his wife, Voula D. Waters, filed suit against USAA in the United States District Court for the Central District of California. The Waters alleged that USAA had breached its duty of good faith and fair dealing under a homeowner's insurance policy by failing to offer adequate reimbursement for the damages that their home had sustained in a fire. They invoked the court's diversity jurisdiction on the grounds

that they are citizens of the State of California and USAA is a corporate citizen of the State of Texas.

3. On July 26, 1991, USAA moved to dismiss the Waters' complaint on the ground that the district court lacks diversity jurisdiction over the case because USAA is an unincorporated association with members in the State of California.

4. On September 9, 1991, the Chief Judge of this Court appointed Judge Laughlin E. Waters (sic) from the Eastern District of Washington to hear this case, since all of the district court judges in the Central District had disqualified themselves.

5. The Waters opposed USAA's motion to dismiss on October 15, 1991, and requested that the district court award sanctions in the amount of $1.72 million for USAA's actions in seeking to dismiss this case from federal court.

6. On February 7, 1992, the district court denied USAA's motion to dismiss and continued under advisement the Waters' motion for sanctions. *See Waters v. United Services Automobile Ass'n*, Civ. No. 91-3615 (C.D. Cal. Feb. 7, 1992) ("Order"). The court also ordered discovery on the sanctions issue and the merits of the Waters' claims, set a May 11, 1992 date for a hearing on the sanctions motion, and a September 14, 1992 date for a trial on the merits.

7. On February 11, 1992, USAA filed a motion in the district court seeking certification of the Order pursuant to 28 U.S.C. § 1292(b) and a stay of discovery. The Waters opposed both motions on February 25, 1992, and the

district court denied them in a telephone conference earlier today. The court denied USAA's certification motion on the ground that this was not an extraordinary case. The court did not separately state its reasons for denying the stay. The court also reset the sanctions hearing for May 14 and the trial for June 22, and ordered that USAA begin producing material in response to discovery by March 16, 1992. (The text of the court's decision is not presently available but will be supplied to this Court promptly upon its release.)

8. This Court is specifically authorized to "issue a stay or injunction pending further consideration of [a] petition [for a writ of mandamus]", *see* Circuit Rules 21-1 to 21-4 Advisory Committee's Note, and has often exercised this authority to preserve the status quo in the district court, *see, e.g., Sunshine Beauty Supplies, Inc. v. United States District Court*, 872 F.2d 310, 311 (9th Cir. 1989); *Arthur Young & Co. v. United States District Court*, 549 F.2d 686, 690 (9th Cir.), *cert. denied*, 434 U.S. 829 (1977); *Kerr v. United States District Court*, 511 F.2d 192, 195 (9th Cir. 1975), *aff'd*, 426 U.S. 394 (1976).

9. In this circuit, "[t]he standard for evaluating stays . . . is similar to that employed by district courts in deciding whether to grant a preliminary injunction." *Lopez v. Heckler*, 713 F.2d 1432, 1435 (9th Cir.), *rev'd in part on other grounds*, 463 U.S. 1328 (1983). A movant is entitled to an order preserving the status quo in a particular case if it demonstrates " 'either (1) a combination of probable success on the merits and the possibility of irreparable injury or (2) that serious questions are raised and the balance of hardships tips sharply in its favor.' " *Tribal Village of Akutan v. Hodel*, 859 F.2d 662, 663 (9th Cir. 1988),

*cert. denied,* 493 U.S. 873 (1989) (quoting *Los Angeles Memorial Coliseum Comm'n v. NFL,* 634 F.2d 1197, 1201 (9th Cir. 1980), *cert. denied,* 469 U.S. 990 (1984)). Under these standards, USAA is clearly entitled to a stay of the district court's proceedings pending this Court's disposition of the Petition.

10. As explained more fully in the Petition, USAA has a strong likelihood of success on the Petition for a number of reasons. First, the district court made a clear error of law in determining USAA's citizenship for diversity purposes because the court declined to apply the Supreme Court's bright-line rule in *Carden v. Arkoma Associates,* 494 U.S. 185, 195 (1990), that a court should, " *'without analysis of the particular entity before it,* count every member of an unincorporated association for purposes of diversity jurisdiction.' " (emphasis added) (citation omitted). The court also declined to apply this Circuit's rule that the citizenship of an unincorporated association is that of its members, *see Rockwell Int'l Credit Corp. v. United States Aircraft Ins. Group,* 823 F.2d 302, 304 (9th Cir. 1987), and persuasive precedents in other Circuits holding with respect to this very defendant that diversity jurisdiction is not available, *see Baer v. United Services Automobile Ass'n,* 503 F.2d 393, 396 (2d Cir. 1974); *Tuck v. United Services Automobile Ass'n,* 859 F.2d 842, 845 (10th Cir. 1988), *cert. denied,* 489 U.S. 1080 (1989).

Second, the district court's Order requires this Court to exercise its supervisory mandamus authority, *see, e.g., Mortgages, Inc. v. United States District Court,* 934 F.2d 209, 212 (9th Cir. 1991), because, without clear guidance from this Court, numerous district courts in this Circuit could follow the district court's rationale in this case and

improperly exercise diversity jurisdiction over unincorporated associations, including USAA. The decision below has already created a conflict within this Circuit on this issue. *See* Petition for a Writ of Mandamus at 20 n. 7.

Third, USAA has no other means of obtaining interlocutory relief from the district court's Order because the district court denied USAA's section 1292(b) motion for certification.

Finally, absent interlocutory relief, USAA would suffer hardship " 'substantially in excess of the usual inconvenience of an unnecessary trial.' " *Varsic v. United States District Court*, 607 F.2d 245, 252 (9th Cir. 1979) (quoting *Pacific Car & Foundry*, 403 F.2d 949, 953 (9th Cir. 1968)). For an indefinite time period, USAA would have to manage its 15,000-case docket under the conflicting directions of the Tenth Circuit, which has directed USAA to move to dismiss all federal diversity litigation, *see Tuck v. United Services Automobile Ass'n*, 859 F.2d at 845 n.3, and the district court, which has ordered USAA to proceed in federal court. Moreover, parties opposing USAA in litigation will seize upon the district court's opinion as justification for improperly bringing state law claims in, or removing them to, the federal courts. These actions would substantially increase the costs for all parties involved.

11. The balance of hardships also tilts in favor of granting the stay because this Court's failure to preserve the status quo pending disposition of the Petition would irreparably harm USAA and would be contrary to the public interest. Unless stayed, the district court's opinion

will encourage counsel opposing USAA and other unincorporated entities to improperly bring state claims in, or remove them to, federal court. Those actions, as USAA has already stressed, would impose unnecessary costs on all involved. Moreover, allowing discovery or other proceedings pending review of the Petition would lead to "undue burden or expense" in this case, *see* Fed. R. Civ. P. 26(c), which would be contrary to the interests of both the parties and the public. Should this Court grant USAA's Petition, all of the parties' and the district court's time, efforts, and money would have been wasted, since the case then would be dismissed for lack of subject matter jurisdiction. Indeed, it appears that the plaintiffs seek to take advantage of the costs to USAA of vindicating its jurisdictional position after trial, for they urge that having tried the matter in federal court, "the likelihood that USAA would retry the entire action rather than settling is virtually nonexistent." Pl. Cert. Opp. at 5 (Appendix to Petition Tab 15). While USAA has no intention of abandoning its jurisdictional position, it should not be forced to undergo useless discovery and trial in this matter before it can reassert a position which is clearly correct.

12. Although the plaintiffs have urged that granting the Petition would not affect their right to sanctions and thus their right to a sanctions hearing, *see* Pl. Cert. Opp. at 3 (Appendix to Petition Tab 15), dismissal of the case would confirm the appropriateness of USAA's motion to dismiss, making an award of sanctions inappropriate. *See, e.g., Soules v. Kauaians for Nukolii Campaign Comm.*, 849 F.2d 1176, 1185 (9th Cir. 1988) (refusing to award Rule 11 sanctions where parties had not acted inappropriately in that proceeding); *Burull v. First Nat'l Bank of Minneapolis,*

831 F.2d 788, 790 (8th Cir. 1987) (same), *cert. denied*, 485 U.S. 961 (1988).

13. Finally, allowing discovery during this interim period would contravene the federal courts' policy of deferring or limiting discovery until such a potentially dispositive preliminary issue has been resolved. *See, e.g., Scroggins v. Air Cargo, Inc.*, 534 F.2d 1124, 1133 (5th Cir. 1976); *Brennan v. Local Union No. 639, Int'l Bhd. of Teamsters*, 494 F.2d 1092, 1100 (D.C. Cir. 1974); *Taylor v. Breed*, 58 F.R.D. 101, 108 (N.D. Cal. 1973); *Kelleher v. Omark Indus., Inc.*, 19 Fed. R. Serv. 2d 725, 727 (D. Mass. 1975). Accordingly, without a stay of all district court proceedings pending review of the Petition, the parties and the public interest would suffer the very harm that the filing of the Petition is designed to prevent.

14. By contrast, entry of a stay would not harm the plaintiffs. The future proceedings in the district court would not illuminate the issues that the Petition raises. Nor would a stay impose any undue burdens on the plaintiffs, because, in this case, they seek only to recover damages for USAA's alleged bad faith in handling their claim. Policy coverage would not be an issue in the proceedings because USAA already has agreed to pay for the reconstruction and repair of the damaged portions of the plaintiffs' home, and that work is almost complete.

15. Preserving the status quo would not unduly delay the proceedings in the court below. USAA has filed its Petition simultaneously with this motion, and is prepared to meet any schedule that this court establishes with respect to consideration of both this motion and the Petition. Accordingly, this Court can ensure that there

would be no undue delay resulting from the entry of an order staying the proceedings in the district court.

## CONCLUSION

For the foregoing reasons, USAA respectfully requests that this Court stay all proceedings in *Waters v. United Services Automobile Ass'n*, Civ. No. 91-3615 (C.D. Cal.), pending review and disposition of USAA's Petition For A Writ Of Mandamus Or Other Appropriate Relief. Pursuant to Rule 27(a) of the Federal Rules of Appellate Procedure and Circuit Rule 27-3, USAA further requests that this Court (a) request an immediate response to this motion from the real parties in interest and (b) rule on this motion on or before March 16, 1992.

Respectfully submitted,

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*Counsel for Petitioner United Services Automobile Association*

February 28, 1992

## CERTIFICATE OF SERVICE

I hereby certify that on this 28th day of February, 1992, I caused to be served one copy of the foregoing Emergency Motion Under Circuit 27-2 for a Stay Pending review of a Petition for a Writ of Mandamus or other Appropriate Relief by hand upon:

William M. Shernoff, Esq.
Shernoff, Bidart & Darras
600 South Indian Hill Boulevard
Claremont, California 91711-5498

Clerk of the Court
United States District Court for
the Central District of California
312 North Spring Street
Los Angeles, California 90012

and by Federal Express upon:

The Honorable Wm. Fremming Nielsen
United States District Court for the
Eastern District of Washington
938 United States Courthouse
Spokane, Washington 99210-2208

/s/ Laurie F. Calder by srr
Laurie F. Calder, Esq.

Counsel for Petitioner United
Services Automobile Association

## 28 U.S.C. § 1332

**§ 1332. Diversity of citizenship; amount in controversy; costs**

(a) The district courts shall have original jurisdiction of all civil actions where the matter in controversy exceeds the sum or value of $50,000, exclusive of interest and costs, and is between –

(1) citizens of different States;

(2) citizens of a State and citizens or subjects of a foreign state;

(3) citizens of different States and in which citizens or subjects of a foreign state are additional parties; and

(4) a foreign state, defined in section 1603(a) of this title, as plaintiff and citizens of a State or of different States.

For the purposes of this section, section 1335, and section 1441, an alien admitted to the United States for permanent residence shall be deemed a citizen of the State in which such alien is domiciled.

(b) Except when express provision therefor is otherwise made in a statute of the United States, where the plaintiff who files the case originally in the Federal courts is finally adjudged to be entitled to recover less than the sum or value of $50,000, computed without regard to any setoff or counterclaim to which the defendant may be adjudged to be entitled, and exclusive of interest and costs, the district court may deny costs to the plaintiff and, in addition, may impose costs on the plaintiff.

(c) For the purposes of this section and section 1441 of this title –

(1) a corporation shall be deemed to be a citizen of any State by which it has been incorporated and of the State where it has its principal place of business, except that in any direct action against the insurer of a policy or contract of liability insurance, whether incorporated or unincorporated, to which action the insured is not joined as a party-defendant, such insurer shall be deemed a citizen of the State of which the insured is a citizen, as well as of any State by which the insurer has been incorporated and of the State where it has its principal place of business; and

(2) the legal representative of the estate of a decedent shall be deemed to be a citizen only of the same State as the decedent, and the legal representative of an infant or incompetent shall be deemed to be a citizen only of the same State as the infant or incompetent.

(d) The word "States", as used in this section, includes the Territories, the District of Columbia, and the Commonwealth of Puerto Rico.

(As amended July 26, 1956, c. 740, 70 Stat. 658; July 25, 1958, Pub.L. 85-554, § 2, 72 Stat. 415; Aug. 14, 1964, Pub.L. 88-439, § 1, 78 Stat. 445; Oct. 21, 1976, Pub.L. 94-583, § 3, 90 Stat. 2891; Nov. 19, 1988, Pub.L. 100-702, Title II, §§ 201(a), 202(a), 203(a), 102 Stat. 4646.)

## Federal Rules of Civil Procedure

### Rule 11. Signing of Pleadings, Motions, and Other Papers; Sanctions

Every pleading, motion, and other paper of a party represented by an attorney shall be signed by at least one attorney of record in the attorney's individual name, whose address shall be stated. A party who is not represented by an attorney shall sign the party's pleading, motion, or other paper and state the party's address. Except when otherwise specifically provided by rule or statute, pleadings need not be verified or accompanied by affidavit. The rule in equity that the averments of an answer under oath must be overcome by the testimony of two witnesses or of one witness sustained by corroborating circumstances is abolished. The signature of an attorney or party constitutes a certificate by the signer that the signer has read the pleading, motion, or other paper; that to the best of the signer's knowledge, information, and belief formed after reasonable inquiry it is well grounded in fact and is warranted by existing law or a good faith argument for the extension, modification, or reversal of existing law, and that it is not interposed for any improper purpose, such as to harass or to cause unnecessary delay or needless increase in the cost of litigation. If a pleading, motion, or other paper is not signed, it shall be stricken unless it is signed promptly after the omission is called to the attention of the pleader or movant. If a pleading, motion, or other paper is signed in violation of this rule, the court, upon motion or upon its own initiative, shall impose upon the person who signed it, a represented party, or both, an appropriate sanction, which may include an order to pay to the other party or parties the

amount of the reasonable expenses incurred because of the filing of the pleading, motion, or other paper, including a reasonable attorney's fee.

(As amended Apr. 28, 1983, eff. Aug. 1, 1983; Mar. 2, 1987, eff. Aug. 1, 1987.)